DOCUMENT RESUME

ED 238 382 HE 016 922

TITLE	Financial Responsibilities of Governing Boards of Colleges and Universities.
INSTITUTION	Association of Governing Boards of Universities and Colleges, Washington, D.C.; National Association of Coll. and Univ. Business Officers, Washington, D.C.
SPONS AGENCY	Kellogg Foundation, Battle Creek, Mich.
REPORT NO	ISBN-0-915164-06-X
PUB DATE	79
NOTE	107p.; Document will be marginally legible due to colored ink on colored pages.
AVAILABLE FROM	Association of Governing Boards of Universities and Colleges, One Dupont Circle, Suite 410, Washington, DC 20036 ($24.95, nonmembers; $13.95, members).
PUB TYPE	Guides - Non-Classroom Use (055)
EDRS PRICE	MF01 Plus Postage. PC Not Available from EDRS.
DESCRIPTORS	Administrator Responsibility; Board Administrator Relationship; *Budgeting; Capital Outlay (for Fixed Assets); *College Administration; College Faculty; *Financial Policy; Financial Support; *Governing Boards; Higher Education; Institutional Characteristics; *Operating Expenses; Purchasing; *Reports; School Accounting; School Maintenance; School Personnel; Trustees

ABSTRACT

A reference manual on financial activities of a college or university and the interactive role of the governing board is presented for board members and institutional officers who provide information to the board. Financial data related to a fictitious hybrid university are included. After identifying three broad kinds of financial information (routine and periodic financial reports, presentations requiring board discussion, and background reports), the following concerns are addressed: the college's overall condition and institutional direction, and external influences. Potential sources of funds and policy issues are considered, along with planning and budgeting concepts needed for a financial strategy. In addition, financial policy issues are discussed concerning faculty and staff, purchasing, maintenance of capital assets, energy, long-term and working capital, fund accounting, and implementing a reporting system. Questions concerning each topic are included. The following types of reports are covered: annual state of the institution, long-range plans and budgets, operating reports, results of operations, and external auditor's report. Sample financial statements, a glossary, and a 36-item bibliography are included. (SW)

****
* Reproductions supplied by EDRS are the best that can be made *
* from the original document. *
****

ED238382

Financial Responsibilities of Governing Boards

of Colleges
and Universities

U.S. DEPARTMENT OF EDUCATION
NATIONAL INSTITUTE OF EDUCATION
EDUCATIONAL RESOURCES INFORMATION CENTER (ERIC)

This document has been reproduced as received from the person or organization originating it.

☐ Minor changes have been made to improve reproduction quality.

• Points of view or opinions stated in this document do not necessarily represent official NIE position or policy.

"PERMISSION TO REPRODUCE THIS MATERIAL IN MICROFICHE ONLY HAS BEEN GRANTED BY

AGB

TO THE EDUCATIONAL RESOURCES INFORMATION CENTER (ERIC)."

Association of Governing Boards
of Universities and Colleges

National Association of College and
University Business Officers

IN 016 922

Copyright © 1979 by the Association of Governing Boards of Universities and Colleges and by the National Association of College and University Business Officers
One Dupont Circle
Washington, D.C. 20036

All rights reserved.

Printed in the United States of America

Library of Congress Cataloging in Publication Data

Main entry under title:
Financial responsibilities of governing boards of colleges and universities.

Bibliography: p.
1. Universities and colleges—United States—Finance. I. National Association of College and University Business Officers.
LB2342.F48 378'.02'0973
78-27710 ISBN 0-915164-06-X

Financial Responsibilities of Governing Boards

of Colleges and Universities

Association of Governing Boards
of Universities and Colleges

National Association of College and
University Business Officers

Sponsored by
W. K. Kellogg Foundation

Contents

Foreword 5

Acknowledgments 5

Preface 6

Introduction 9

Chapter 1: Context for Financial Planning and Management 13
Overall Condition and Institutional Direction 13
External Influences 13

Chapter 2: Generating Financial Resources 20
Students 20
Governmental Sources 23
Private Sources 26
Institutional Sources 27
Sales and Services 29

Chapter 3: Spending Financial Resources 31
Faculty and Staff 32
Purchasing 38
Maintenance and Replacement of Capital Assets 39
Energy 40

Chapter 4: Managing and Protecting Financial Resources 43
Working Capital 44
Long-Term Capital 50
Total Capital 55
Protecting Resources 56
Guide to Fund Accounting 57

Chapter 5: Planning and Budgeting 60

Chapter 6: Implementation 65

Illustrative Exhibits 89

Glossary 99

Bibliography 102

Foreword

This monograph was developed over a period of more than two years by a joint steering committee of the Association of Governing Boards and the National Association of College and University Business Officers. The steering committee was composed of three trustees, three presidents, and three business officers, whose names appear in the acknowledgments.

Eight pilot test institutions participated in the project; their boards and administrators evaluated an early draft of the monograph and reviewed the concepts and principles described therein with respect to financial information from their own institutions. These steps were important in refining the monograph. More than five hundred copies of a subsequent draft were sent for review to trustees, presidents, and business officers from many types of colleges and universities; the comments received resulted in substantial improvement in the final version.

The boards of directors of the two associations have approved this monograph for publication. They recommend it to their members and to all others interested in the financial information needs of governing boards. However, implementation will require careful consideration, evaluation, and adaptation to each institution's particular needs. It is recognized that there is no single approach suitable for all institutions or even for one kind of institution, but it is stressed that the concepts and principles emphasized in this monograph and the suggested approach for financial reporting will serve as helpful guides.

The associations hereby commend the steering committee members for their extraordinary involvement in this project.

Robert L. Gale
President
Association of Governing Boards
of Universities and Colleges

D. F. Finn
Executive Vice President
National Association of College and
University Business Officers

Acknowledgments

This monograph was made possible by a grant from the W. K. Kellogg Foundation, of Battle Creek, Michigan. The Association of Governing Boards and the National Association of College and University Business Officers are especially grateful to Dr. Peter R. Ellis, program officer of the foundation, for his strong and abiding interest in the project, from proposal to publication.

The steering committee was composed of three trustees, three presidents, and three business officers, but the committee was much more than the name implies. The members worked for two years in planning the project, reviewing several drafts and hundreds of comments, and making recommendations for revision. This monograph is the result of their dedication. The members:

- John W. Pocock, Chairman of the Board of Trustees, The College of Wooster, *Chairman*
- James F. Brinkerhoff, Vice President and Chief Financial Officer, The University of Michigan
- Merrill A. Ewing, Treasurer and Business Manager, Mount Holyoke College
- Darrell Holmes, President, East Stroudsburg State College
- Elmer Jagow, President, Hiram College
- Robert E. Lahti, President, Community College of Denver
- Mary Louise Petersen, President, Iowa State Board of Regents
- Frank Smathers, Jr., Trustee, University of Miami
- William M. Wilkinson, Director of Finance, The University of Rochester

Coopers & Lybrand, certified public accountants, provided substantial funds as well as a group of consultants, headed by Wallace E. Ackley. The consultants undertook the initial research, helped to organize the monograph, and offered guidance to the directors and steering committee at each stage of the process.

Codirectors of the project were Nancy R. Axelrod, of AGB, and K. Scott Hughes, of NACUBO. They managed the project, coordinated the several reviews, and revised the various drafts. Their role was far greater than that of directors only.

Also to be acknowledged are Douglas J. Collier, of the National Center for Higher Education Management Systems, who served as a consultant to the project and who wrote much of Chapter 1; Abbott Wainwright, of NACUBO, who edited the final manuscript for publication; and Mariise Mason, who designed the monograph.

One of the most important contributions was participation of the governing boards of eight pilot test colleges and universities, without which the practices recommended in the monograph could not have been tested. These institutions are listed below with their liaison officers, who devoted many hours to this project.

- The University of Alabama, David W. Phipps
- California Lutheran College, A. Dean Buchanan
- Dallas County Community College District, Walter L. Pike
- University of Delaware, J. Robert Harrison
- Indiana University of Pennsylvania, George W. Murdoch
- Lawrence University, Marwin O. Wrolstad
- University of Miami, John L. Green, Jr.
- Ohio Wesleyan University, Robert W. Meyer

Although unnamed here, over 200 reviewers provided comments on the various drafts of this monograph. Their participation, which is hereby acknowledged, was essential to the success of the project.

Preface

Financial pressures affect almost every aspect of an institution's programs. Each program action taken is related to the institution's finances, and the availability of financial resources is a dominant factor in setting institutional priorities. Although there are some differences in the governance process between public and independent institutions, the governing board carries the ultimate authority and responsibility to guide the destiny of the institution, including the assurance of continued financial viability.

The proficiency with which members of governing boards exercise this stewardship depends critically on their understanding of the financial affairs of the institution and on how effectively significant financial information is communicated to them. But the apparatus for communicating such information in a manner to enhance their decision making appears to need some improvement.

Inquiries directed to the Association of Governing Boards frequently come from trustees and regents who have difficulty in interpreting the financial information presented to them. Trustees without a background in finance (and, traditionally, not included on finance committees) acknowledge embarrassment in asking questions that reflect this inexperience, yet they recognize their responsibility to participate intelligently in financial decisions. Even board members with financial experience in other fields often question the peculiarities of college and university finance.

This concern of board members has not gone unrecognized. Several attempts have been made by public accounting firms and individual colleges and universities to change the manner in which financial information is communicated to the board. Useful notions have been developed but, by and large, the suggestions center on technical adjustments in the manner in which financial information is conveyed rather than on the management decision needs of boards. As a body, the trustees and regents have yet to be heard from; this monograph approaches the information problem from their point of view.

The reader should be aware of two major thrusts. First, the monograph is directed to members of governing boards. Although procedures and reports are suggested, the basic objective is to trace in clear and simple terms the dynamic, continuous flow of financial resources through the programs of the institution. This flow moves from the acquisition of funds through allocation and operating expenditure to the protection and enhancement of the institution's capital. The attempt to reduce the presentation to basic concepts and terms will inevitably bring charges of oversimplification from the financially astute practitioners; their indulgence is requested on behalf of the less experienced trustee. Second, the monograph stresses the use of financial accounting information for managerial rather than fiduciary purposes. Relevance of financial outcomes to program decisions is noted. Policy items relating to financial decisions are stressed. Ways are suggested to use the information for analyzing performance in achieving objectives, and some key financial indicators are proposed. The position is taken that administrative officers have an obligation to communicate financial information continually to the board to permit trustees and regents to intelligently monitor the financial status and progress of the institution and its programs.

The monograph includes other aspects of the board's obligations only as they relate to financial consequences. It is designed as a reference manual useful both to board members and to institutional officers who provide information to the board.

Caveats and Limitations

Any attempt to portray the complex financial activities of a college or university and the interactive role of the governing board is necessarily ambitious. A major limitation is the extreme diversity of institutions. This monograph does not categorize the many characteristics that make institutions different from each other, but some of the major institutional differences that will affect adaptation of the material in this monograph are listed below.

Public/Independent. While governing boards of independent institutions are the ultimate decision makers, boards of public institutions may be accountable to a combination of state boards, commissions, the budget office, and the legislature. However, it is generally a responsibility of the board of a public institution to reconcile, integrate, and implement the policies of these agencies; that is, the board should be the managerial center for the agencies. (Although it is recognized that governing boards of public institutions may not have the degree of control that boards of independent institutions have, this monograph refers to boards as if they all had ultimate control.)

Level of Involvement. The monograph assumes that a governing board, when addressing financial issues, is concerned primarily with (1) approving the institution's mission, goals, and policies, (2) reviewing institutional activity, and (3) evaluating institutional performance with respect to objectives. However, there are institutions—notably, many community colleges—where the board takes a more active and detailed approach to its overseer responsibilities. The degree of involvement a governing board has with the management of the institution will determine the kind of financial information it requires.

Governing Board Organization. Design of the board's financial information system depends on (1) size of the board, (2) committee organization, and (3) frequency of board meetings. Each board, with the administration, should determine its financial information requirements, using the guidelines contained in this monograph.

Importance of Specific Financial Issues. The mission of an institution is often a guide in determining what financial information is most important for its governing board. The relative importance of each financial issue may vary over time; certain issues may not change for many years, while others, such as tuition and admissions, may always require attention.

Internal Management and Financial Information. Because the monograph focuses on financial information for governing boards, there is little mention of the organization of financial information required by the administration for routine internal operations or of the data-gathering systems that institutions use to prepare the financial reports. Information used by the board comes from several sources, such as the president and his or her staff, chief academic officer, chief business officer, student affairs officer, development officer, registrar, etc. Implementing a comprehensive system to gather the information required by the board will take time; a team approach is thus recommended for efficiency with respect to both time and overlapping responsibilities.

Standards

While the monograph recommends standards of good practice such as establishing policies and having a long-range plan, no attempt has been made to establish performance norms. The monograph does suggest that the exchange of financial information with similar institutions can often serve as a substitute, if not an improvement, for any attempts to establish normative standards of performance. Such an exchange must be implemented with great caution, and the differences in institutions must be considered. There is no single standard of financial performance, due to the uniqueness of each institution.

Hybrid University and Other Examples

The monograph contains financial and statistical data related to a fictitious Hybrid University. The data are generally consistent throughout, so the reader should be able to develop an understanding of the financial strengths and weaknesses of Hybrid University. The source of financial data is Chapter 5:7, "Illustrative Exhibits," of NACUBO's *College and University Business Administration* (1974), reproduced herein under the same title immediately following Chapter 6, "Implementation."

Use of the Monograph

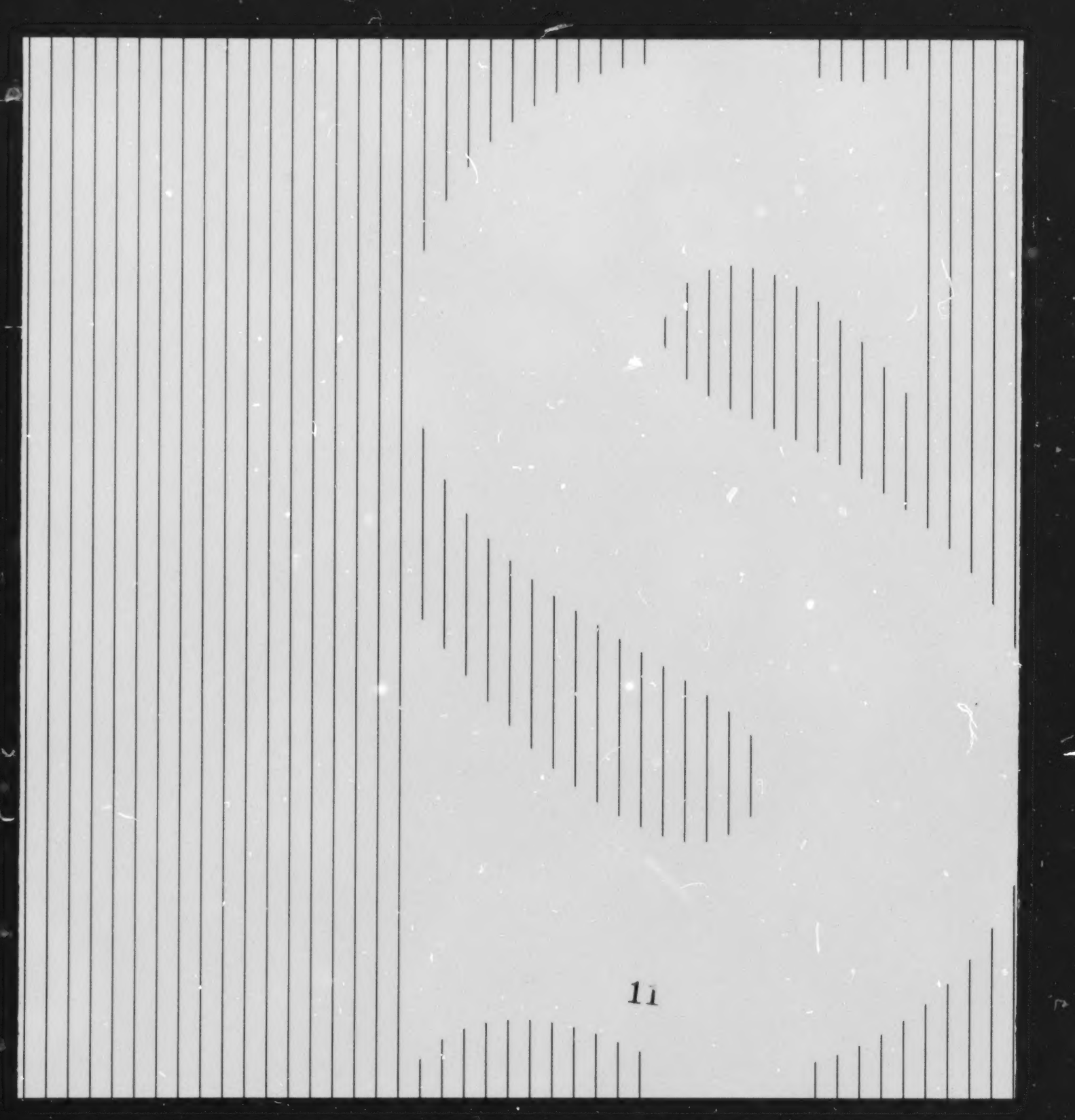
It should be stressed that in trying to encompass *all* types of institutions, this monograph naturally raises more questions than need to be asked about a *specific* institution. Because its scope of potential issues is so broad, trustees are cautioned that all the "Suggested Questions" highlighted in the monograph do not need to be asked of, and indeed cannot be answered by, the management of a specific institution. Rather, issues facing the institution must be placed in order of priority.

Trustees should be sure that the questions they raise are not related to issues that would be "nice to know" for their institution, but are those that would have a significant effect if the information were available for decision-making. Business officers reading this monograph may be overwhelmed at the potential questions that trustees might raise and may be reluctant to encourage trustees to give full attention to careful deliberation of the issues, concerns, and questions raised in the monograph—not through unwillingness to be responsive, but because of the potential burden of preparing responses by an already overworked staff.

There is no easy answer to the needs of trustees, on the one hand, and the ability of the institution to respond economically, on the other. It is hoped that this monograph will serve as a reference point for discussion among trustees, the president, academic officers, and business officers to enable them together to direct their attention more effectively to major issues facing their institution and to develop economical ways to provide information useful for decision making.

Suggested reports have been designed at an elementary level, as there is no single model of reports that could be used by all institutions; reports should be designed to fit the needs and available information of the particular institution.

This monograph will have been a success if it encourages open, frank discussion among the trustees, president, and other administrators. It is urged that administrators be aggressive in encouraging trustees to study this monograph, but trustees are cautioned to be moderate and conservative in imposing demands on the institution without understanding the costs and value of providing the information.



Introduction

One purpose of this monograph is to suggest how financial information should be presented to the governing board. Instrumental to the presentation of such information is an efficient communication system, which ultimately depends on the relationship between the board and the institution. The key persons in this relationship are the chairperson of the governing board, chairperson of the finance committee (if there is one), and the president and the chief business officer of the institution. Close cooperation among these persons is essential for financial information to flow freely in both directions.

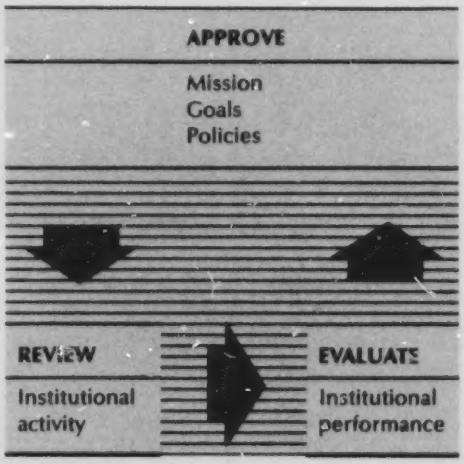
The monograph stresses the importance of a clear statement of board organization and of how the board should function. The organization of the institution should also be clearly defined and the authority and responsibilities delegated to the president should be well documented. The officers of each major unit, usually vice-presidents, should have an understanding of their roles and responsibilities with regard to the board as a whole and to its committees.

How the board is organized is less important than having clearly defined responsibilities for board members and having a board that is dedicated to the academic and financial success of the institution. The board must rely on the president to initiate the management process, but because of its position, the board has the ability to provide the following:

- **Strong leadership.** Since the board typically has ultimate responsibility for the financial well-being of the institution, it is in a position to encourage establishment of sound financial management systems.
- **Different perspectives.** Governing board members have broad and diverse knowledge of many kinds of organizations; such knowledge affords valuable perspectives for colleges and universities.
- **Resources for the future.** Because the board is insulated from routine operations, it can focus on the future of the institution. One of its primary responsibilities is to make decisions and to take actions that will protect and enhance the institution's resources for the use of future students; this requires the delicate balancing of resources between the present and the future.

The approach used in this monograph for describing how a governing board oversees the institution's affairs is illustrated in the accompanying figure. This approach involves board responsibility at three levels of the management process:

1. **Approving** institutional mission, goals, and policies.
2. **Reviewing** institutional activity.
3. **Evaluating** institutional performance in meeting objectives.



To carry out these functions effectively, the governing board requires different kinds of information and should devote different amounts of time to each. Primary attention should be directed to reviewing and approving mission, goals, and policies. With clearly defined objectives, review and evaluation can focus on major problems, requiring less time.

Kinds of Financial Information

The way in which financial information is presented to the governing board depends on the purpose of the information and on what action the board is required to take. For example, such information can range from a routine report on new gifts received to a complex presentation of the long-range plan, involving many participants, visual aids, and long discussion.

Financial information can be separated into three broad categories:

- **Routine and periodic financial reports.** Communication for this purpose is generally in one direction: from the institution to the governing board. It may include reports on gifts received, new faculty appointments, and single purchases above a given dollar amount. The board is generally asked to ratify these matters, and little discussion is required.
- **Presentations requiring board discussion.** Communication in this case involves active participation of both parties. The administration makes a presentation, with recommendations to the board, for eliciting the board's judgment and ultimately its approval. Such matters as policy formulation, long-range planning, budgeting, and the purchase and sale of real property require this type of exchange.
- **Background reports.** As will be mentioned in Chapter 1, the board should be given reports describing the environment in which the institution operates. Such reports are for information only, and no action is expected to be taken on them; their purpose is to provide background material for decisions to be made at subsequent board meetings. This kind of information addresses the need for the board to examine and understand change, and thus to help the institution adjust to changes in the environment. It does not focus on any

particular function, such as budgeting, or on any operating unit. Rather, it is provided because the board should be kept informed of happenings that may affect the institution and thereby its finances. The information presented may indicate trends that would lead the board to ask for more details. A corollary purpose of this kind of information is to prevent the board from being surprised when events occur that require a change in plans or operations.

The governing board and the institution's officers have the combined responsibility of designing a communication system that groups financial information in a manner that meets the board's needs. This can be accomplished by jointly identifying those subjects requiring only routine reporting and those focusing on more complex issues requiring the judgment and approval of the board.

Context and Consequences of Financial Information

When the governing board makes judgments on issues and ultimately approves policies, plans, and budgets, the financial information provided for these purposes is critical. If presented properly, such information will be illuminating and helpful; if presented poorly, it can be boring and sterile, or complex and confusing. The problem, of course, is what constitutes "proper" presentation. Boards should be given the context of the information, with a clear statement of the prospects, as well as the information itself. Some examples are presented below, where the second alternative is preferred to the first.

Alternative 1: Tuition income for this quarter is $1.2 million.

Alternative 2: Tuition income for this quarter is $1.2 million, down two percent from a year ago, but in accordance with the budget. However, tuition from entering freshmen is five percent less than estimated, which was offset by a 10 percent increase in tuition from transfer students. The decrease in entering freshmen is of concern and is being analyzed by the dean of admissions.

Alternative 1: Investment performance matches the goal for the fiscal year.

Alternative 2: Although investment performance matches the goal for the fiscal year, there are disturbing indications that the recent rise in interest rates may have an adverse effect on the institution's investment in common stocks.

Governing boards, when given the *context* of the data and any related prospects, will be more effective and will respond more quickly to recommendations of the administrators. Some factors appropriate for placing an issue in its proper context and describing the consequences may be:

1. Time span. Context: What has happened over time? (Example: Continual increases in tuition.) Consequences: What effect has this caused? (Example: Continual need for more student aid funds.)

2. Policies and goals. Context: How does the issue relate to existing policies and goals? (Example: Decrease in the expected return on endowment compared to the amount budgeted.) Consequences: What effect does the issue have on the institution's policies and goals? (Example: The amount budgeted for endowment income must be decreased, which increases the estimated deficit.)

3. Environmental factors. Context: How does the issue relate to external conditions? (Example: The increase in utility costs caused by rising oil prices.) Consequences: How is the issue affected by external conditions? (Example: Implementation of energy-saving measures to partially offset increase in energy costs.)

4. People. Context: Does the issue affect students, faculty, staff, alumni, and general public? (Example: Level of tuition affects students, parents, and general public.) Consequences: What effect does the issue have on these people? (Example: Students and parents will have to pay higher tuition.)

An analysis of both the context and consequences of issues taken to the board is necessary for an effective and active board.

Presentation of Financial Information

Whether the subject is a routine report of federal grants and contracts received or a complex issue such as approving the operating budget, governing boards should be provided with financial information that focuses on critical issues in a manner that is logical, clear, and concise. There should be continual awareness of not overburdening the board with information. For smooth and effective communication, there are three rules for administrators to follow in presenting financial information to the board. These are:

- **Focus on the issue.** There should be no ambiguity on why a subject is being discussed. Board members should know if they are being asked to approve, review, or evaluate the subject.
- **Include the context and consequences.** (The previous section discussed the importance of this rule.)
- **Present the information in a logical sequence.** The presentation of financial information should begin at the governing board's point of reference and should bring the board step-by-step to the point at which a decision can be made. A traditional approach used for effective presentation is:

a. Statement of the problem.
b. Background information.
c. Statement of approach to the problem, and

assumptions used.
d. Description of form of analysis used.
e. Description of feasible decision alternatives and their consequences.
f. Recommendation and justification for the alternative chosen.

The amount of time spent on each part of the presentation depends on the complexity of material and the level of familiarity the board has with the issue. For example, the board (or investment committee) may be very familiar with the subject of investment policy, so the presentation of that subject could be brief. However, other subjects such as facilities planning, new academic programs, and setting tuition may require more time on background, assumptions, and description of the analysis, involving visual aids and lengthy presentations.

Board Meeting and the Agenda

The board meeting is the forum in which members of the board officially assume their roles as overseers of the institution and legally act in that capacity. For the board to be effective, the meeting should be well planned and actively managed. There are several ways to help assure an effective board meeting. One of the most critical items is the agenda; its preparation can mean success or failure for a board meeting. A well-planned agenda can be a catalyst to crisp action; conversely, a poorly conceived agenda can cause confusion, frustration, and inactivity.

The following will help to assure effective presentations:

1. There must be adequate time to prepare the agenda. Administrators should develop a schedule that allows adequate time for preparing agenda items. This includes staff time for data accumulation, analysis, documentation, report presentation, and internal review and approval. Agenda items not subjected to this rigorous process are susceptible to poor presentation and unanticipated questions from board members. Particularly complex issues may require that the institution's officers prepare very carefully if effective presentations are to be assured. The chairperson of the board and chairpersons of its committees should also be fully briefed in advance of the meeting.

2. Only major issues should be presented. The board meeting should be planned to minimize the routine and to focus on critical issues. The agenda should be organized so that only major items are given priority at the board level.

3. The agenda should be distributed in advance. The agenda and supporting documentation should be received by the board at least a week before the meeting. It is especially important that financial reports be received well in advance. To the greatest extent possible, items not on the agenda should be prohibited from being presented at the meeting; it is usually better to defer an item to the next meeting rather than to present it with no warning.

4. Resource persons should be used. Institutional officers and consultants can often enrich board presentations and should be used to full advantage. Although the president must be the leader, he or she can often effectively delegate presentations or refer specific questions to resource persons.

As the issues presented to the board have become more complex, some boards have established ad hoc committees for certain subjects such as review of the operating budget, long-range planning, and debt financing. The ad hoc committee meets with the institution's management team for a detailed discussion of the issues. Such sessions are rewarding to both the board members, who become more knowledgeable, and the institution's officers, who receive a different perspective on key issues. When the issue comes to the full board, ad hoc committee members can contribute much to the discussion.

Another key ingredient for successful board meetings is an understanding on the part of the academic administration of the financial issues facing the college or university. Such an understanding can be accomplished only through close teamwork by the academic and financial administrators. Board presentations that have the full participation of both academic and financial administrators will be more complete and will more likely reflect the overall goals of the institution.

Cycle of Financial Reporting to the Board

Issues taken to the board in a logical sequence and related to previous and future issues will give the board a further awareness of the time span and frame of reference for the decisions at hand. For example, the planning and budgeting process is continuous. This means that the sequence for establishing the plan, adopting a budget, and continually reviewing performance in meeting objectives should be well defined, with a clear understanding of the specific issues to be brought to each board meeting.

The governing board and the institution's administrators should jointly develop a calendar of decision issues that lists items to be presented to the board. Such a calendar provides continuity and stability, but administrators must balance the routine with the nonroutine. Not all issues to be presented fit neatly into a planning calendar; the board and administrators should establish a management approach that can respond in a timely manner to issues of immediacy. Even in urgent cases, care must be taken that the decision issue has been well defined and analyzed, with only well-considered recommendations presented.

Context for Financial Planning and Management

Chapter 1

As part of the context in which financial decisions are made, governing boards often discuss such issues as the institution's financial strength and stability, a changing student clientele, collective bargaining, demands for accountability, and inflationary pressures. However, it is important that they understand how these issues interact in their effects on the institution and that they consider these effects as part of the planning and management process.

The following questions are addressed in this chapter:

- What is the institution's current overall condition, and is the institution moving in a desirable direction?
- What factors in the external environment might affect the institution?

Both questions should be examined in their relation to the mission. In regarding the two questions, one assumes that the governing board should know the answers prior to conducting the long-range planning and budgeting process. Therefore, this chapter might be viewed as describing the framework for a "state of the institution" report. Such a report would be prepared on an annual basis and would provide an up-to-date context for both planning and budgeting decisions (see Report No. 1 in Chapter 6). It would include (1) an assessment of the current overall condition of the institution and the direction in which it is moving, with particular emphasis on how the past year's operations affected that direction, and (2) a list of environmental factors expected to have (or that are now having) significant effects on the institution.

Overall Condition and Institutional Direction

Ideally, every college and university moves in a direction consonant with its mission. Each time the institution accepts a new class of freshmen, the kinds of students it accepts have a significant effect on what the institution is and where it is going for at least the next four years. (For example: Do the students require financial aid? Are they academically strong or weak?) The hiring of faculty members and the granting of tenure can affect the institution for many years into the future.

It has been argued that no one person or governing board actually changes an institution. Rather, the board and the president, with the participation of the faculty, lead the institution in the direction it should go as decisions regarding change are made. Perhaps the most obvious way to lead an institution is to decide where, and in what ways, changes are to be made in program and personnel. But even in a more or less steady state, decisions (not necessarily changes) are made every day that affect institutional direction. Colleges and universities inevitably change, and the direction of that change is a legitimate concern of the board.

To analyze overall condition and institutional direction, this chapter focuses on more than financial data. The assumption is made that it is just as important to know that the "demand" for the institution's services remains strong (or, from the institution's perspective, that it has sufficient "drawing power") as it is to know that the balance sheet reflects a better financial condition each year. The following factors may be used to analyze condition and direction of movement:

1. Drawing power.
2. Structured learning environment.
3. Non-classroom learning environment.
4. Financial strength.
5. Outcomes.

Drawing Power

In a college or university, as in any enterprise, it is important that the demand for its services be strong if it is to remain in good overall condition. In considering overall condition and direction of institutional movement, the concept of "drawing power" will be used to connote the institution's perspective regarding the demand for its services. The board is responsible for generating attractiveness through diversity of programs and other means.

Drawing power may be defined as the ability of the institution to attract a desired market for its educational services, for donor support, and for a superior faculty. It includes the ability to attract the kinds of students it considers itself to be serving and to provide the kinds of research and public services for which it has the capabilities. When one considers drawing power, the focus should be on ability to attract the *kinds* of students, research projects, and public service programs the institution desires as well as the *number* of students, research projects, and so forth. Or in a more active sense, drawing power suggests the ability of the institution to "sell" its services in the quantity, and at the price, it desires.

For assessing *overall condition*, drawing power can be viewed as a measure of the institution's potential for attracting revenues. In certain kinds of institutions, it can also be seen as a concept parallel to selectivity, that is, the ability of the institution to be selective about the types of students it chooses to admit, the types of faculty it chooses to hire, and the types of programs it decides to conduct. While student selectivity obviously means little for institutions having "open admissions," for those institutions that desire to be selective, a change in their ability to be selective can be regarded as a measure of change in their drawing power.

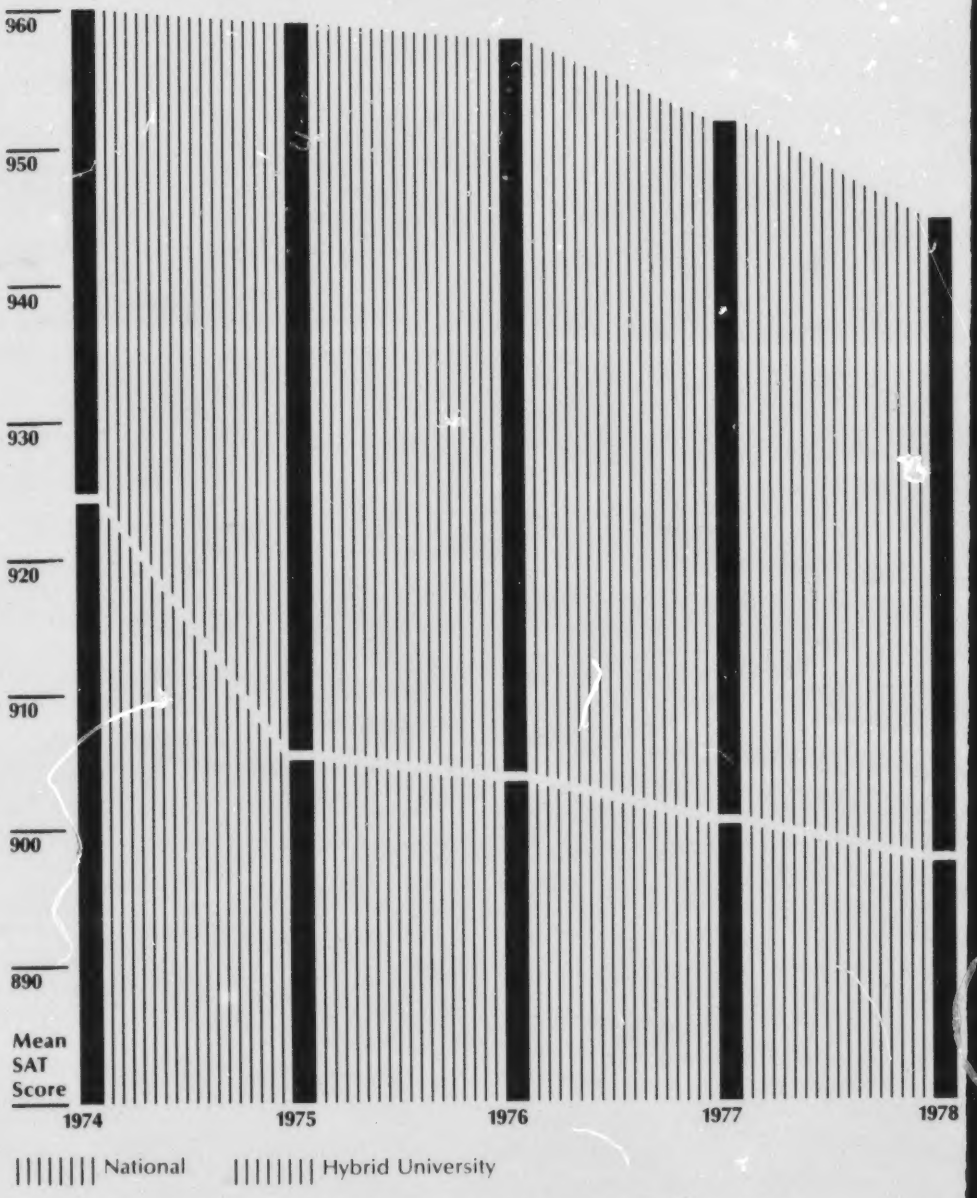
Drawing power can have a significant effect on the type and amount of financial resources the institution has available for use; for example, it affects the number of students paying full tuition, number and kinds of grants the institution receives, and the willingness of donors to make gifts. Drawing

power also affects other aspects of overall condition such as financial *flexibility* (Is the institution attracting revenues that can be used for several different purposes?), financial *independence* (What is the "mix" of sources of revenue the institution is attracting?), and financial *risk profile* (What is the certainty of funding associated with the various sources of revenue?).

For assessing *institutional direction*, drawing power can be related to the types of students and research projects or public service programs the institution is attracting. For example, changes in characteristics of students entering the institution will affect its direction of movement. One of the decisions institutions make that affect their ability to draw students involves admissions criteria (or in the case of open admissions, the existence of an "open" criterion). For example, if an institution decides to significantly change its entrance requirements, a different kind of student will be drawn to the institution and its direction of movement will change. Another change related to drawing power may not even involve an explicit decision; for example, if the institution begins serving for the first time a significantly large number of part-time students through evening classes and nontraditional programs, the direction of movement is affected.

Mean Scholastic Aptitude Test (SAT) Scores

for Entering Freshmen at Hybrid University



Source: Higher Education and National Affairs, *September 15, 1978 (vol. XXVII, no. 36).*

Suggested Questions

1. How do academic characteristics (e.g., SAT scores and high-school class standing) of students currently applying compare with those of applicants in prior years? (See Report No. 1 in Chapter 6.)

2. How many applicants have to be accepted to enroll one student? How has this ratio changed over the last few years? (See Report No. 1 in Chapter 6.)

3. How many students are applying to the institution this year compared with previous years?

4. How many students remain from one year to the next, e.g., from freshman to sophomore, and how does this compare with previous years? (See Report No. 1 in Chapter 6.)

5. How many research proposals are submitted by the faculty for each grant that is received? How has this ratio changed over the last few years?

6. What kinds of research and public service projects are being undertaken now compared with five years ago?

7. Is it difficult to attract well-qualified faculty members?

8. Is donor interest being maintained?

Structured Learning Environment

A second element of the institution's overall condition is the quality of its structured learning environment, which for this analysis is defined to include the set of conditions that facilitates or impedes the ability of students to learn as part of a structured learning process. In this chapter it is hypothesized that the "quality" of a student's educational experience is a product of, and the interaction between, the institution's structured learning environment and its non-classroom learning environment. The proposed "state of the institution" report mentioned earlier asks the governing board to assess the quality of these two environments separately as a proxy for assessing the quality of the educational experience provided by the institution. (The non-classroom learning environment is discussed in the next section.)

In assessing the structured learning environment as part of the analysis of *overall condition*, the governing board should ascertain the existence or absence of a "collegial" atmosphere between faculty and students and between faculty and the administration, the quality of the faculty, and the availability of educational support staff and other supporting resources such as equipment and library resources. In assessing the structured learning environment as it relates to *institutional direction*, the same factors would be considered, but the focus would be on the *changes* that have occurred in each area over time.

Suggested Questions

1. Have recent accreditation reviews of the institution's departments resulted in any recommendations for significant changes? If so, what kinds of changes were recommended? Have they or are they being implemented? If not, why not?

2. What are the percentage distributions of faculty within the various departments by tenure and nontenure?

3. How adequate are the library resources in providing support for the various departments? How adequate are other support items (media, computer, facilities, staff) for each of the departments?

4. Do the institution's various departments have particular areas or specialties in which they have a national or regional reputation?

5. What are the number and nature of awards and honors that have been received by students, faculty, and staff? How do they compare with those of past years?

6. Have turnover rates of faculty and staff changed significantly over the last five years? What has been the student attrition or dropout rate for the institution as a whole and for its departments?

7. Is the compensation of faculty and staff competitive?

8. How have faculty been rated on the student evaluation survey? How does this rating compare to ratings of past years?

9. Is the faculty unionized or are unionization efforts under way? Are demands outlined in union proposals more or less consistent with the institution's goals and objectives than they were in the past?

Suggested Questions

Non-classroom Learning Environment

Another important contributor to the student's learning experience in most institutions (at least in those providing some type of learning experience outside the classroom) is the non-classroom learning environment, which for purposes of this analysis may be defined as the set of conditions that facilitates or impedes the ability of students to learn from others as well as to educate themselves *outside the classroom*. As such, it includes the aggregate of social, cultural, and living conditions to which the student is exposed. It can be characterized by social and cultural diversity of the student body, diversity and type of living arrangements available to students, environment created by physical surroundings of the campus, and number and range of organized social and cultural opportunities available—for example, concerts, athletic events, theatrical productions, and guest lectures.

In assessing the non-classroom learning environment as part of the analysis of *overall condition*, the governing board should consider (1) the existence of opportunities (or lack of them) for learning outside the classroom as well as the range of such opportunities available to students, (2) condition of the physical plant (whether it is being adequately maintained or is deteriorating), (3) relevance of the physical plant for the kinds of educational programs the institution is providing, and (4) the extent to which the social and cultural diversity of the student body is consistent with the institution's mission.

In assessing the non-classroom learning environment as part of the analysis of *institutional direction*, the board should check to see if there have been any significant changes in these same factors over time.

1. Is the student body sufficiently diverse (e.g., in its social and cultural characteristics) to promote the kinds of non-classroom learning experiences the institution desires? Has the diversity of the student body changed significantly over the last five years?

2. Are annual expenditures for maintenance and renovation of the physical plant sufficient to keep the buildings and grounds adequately maintained? Has the level of those expenditures kept up with plant additions, obsolescence, and inflation in the last five years?

3. What kinds of organized non-classroom learning experiences (e.g., concerts, guest speakers, social events) are currently being provided? What is the level of financial support for such activities? Has either the level of financial support or the number and type of such activities changed significantly in the last five years? Are there adequate facilities for the activities? Are there opportunities for volunteer experiences in the community?

Financial Strength

The fourth aspect to be considered in overall condition and institutional direction is financial strength. While colleges and universities are not in the business of "making money" as their primary objective, they must nevertheless have money to operate.

In higher education it is important, at least for independent institutions, for revenues to exceed expenditures in some years; the remaining revenues can be used to carry the institution through years in which expenditures exceed revenues (see Report Nos. 16 and 18 in Chapter 6). Provision for the future from excess revenues generated in present operations is such an integral part of the financing strategy of most independent institutions that it can be viewed as one criterion for evaluating financial strength. If an institution is unable year after year to save some portion of current revenues for future working capital and plant needs, it will soon have no reserves to draw upon when needed.

There are essentially three questions regarding this aspect of the institution's operations:

1. Is the institution living within its means on a year-to-year basis?
2. Are the institution's various sources of revenue stable?
3. Is the institution providing itself with financial resources it can draw upon to support future operations?

In addition to the assessment of *operations*, a financial analysis should consider the institution's *assets*. In analyzing assets one should give attention to (1) the adequacy of those assets relative to the amount and type of assets needed to carry out the institution's programs and (2) the flexibility with which those assets can be employed should financial difficulties arise. (See Report No. 15 in Chapter 6.)

Suggested Questions

1. Have the net changes in fund balances been positive? (See Report Nos. 16 and 18 in Chapter 6.)

2. At what level, and with what certainty, will the institution's primary sources of financial support continue to provide funds in the future?

3. Has the institution been able to set aside unrestricted revenues to serve as quasi-endowment funds? What is the current amount of such funds? (See Report Nos. 16 and 18 in Chapter 6.)

4. What percentage of the institution's assets can be liquidated and expended should the need arise? What problems would be encountered in doing so? (See unrestricted fund balances in Report No. 15 in Chapter 6.)

Outcomes

The final element in the governing board's consideration of overall condition and institutional direction involves assessment of the "outcomes" of the institution. A major outcome of colleges and universities is the educated student; unfortunately, this outcome cannot be measured directly.

Outcomes are probably more relevant to institutional direction than to overall condition. For example, if such outcome indicators as average scores on the Graduate Record Examination (GRE) for graduating seniors or the percentage of graduates obtaining employment change significantly over time, the board would want to study what is happening in more detail. (Some would say that GRE scores are an indicator of the quality of the instruction program. However, in the context of this monograph, GRE scores would be considered only as an indicator of institutional direction.)

Information about outcomes is usually not collected routinely by institutions because it is difficult to do; tangible indicators are few and subjective judgments are often biased. To obtain such information as the percentage of graduates obtaining employment or percentage of graduates continuing their education, it will often be necessary to survey graduating students.

Suggested Questions

1. Has the percentage of graduates either obtaining employment or continuing their education changed significantly in the last five years?

2. How has the percentage of students who complete their programs in the normal time changed in the last five years?

3. In the case of community colleges, how many students transfer to senior institutions?

4. How have the Graduate Record Examination scores of graduating seniors changed by majors over the last five years?

External Influences

In addition to considering overall condition and institutional direction, a second topic to be considered in establishing the context for planning and management relates to the effect of the external environment on the institution. Current environmental factors affecting colleges and universities include general economic conditions, increasing inflation, more demands for accountability, changing national and regional enrollment patterns, energy costs, collective bargaining, government regulations and reporting requirements, and a leveling of financial support.

Most governing boards are aware of these external factors, which should be understood in the context of opportunities as well as constraints. The external constraints on the institution's actions are obvious, such as legal requirements and limits of financial support available, but boards should not overlook the *needs and opportunities* within the environment that the institution can exploit.

For most colleges and universities, needs are met and opportunities are provided through three primary programs: instruction, research, and public service. Needs and opportunities can be viewed in a framework of those programs, namely, those related to instructional programs (which the institution currently provides or has the capability to develop), those related to research capabilities and interests of the faculty, and those related to public service programs the institution conducts.

With respect to external conditions, an institution may find that a changing student clientele may result in declining enrollments of traditional students while it also creates opportunities for providing instructional programs on weekends or at night to nontraditional students; for example, retraining, licensing, certification, and other nondegree activities are increasingly required in a complex society. And while the energy crisis has raised the institution's energy costs, it has also created new educational and research opportunities.

Environmental constraints affecting the institution's freedom of action are competitive, economic and legal. Decisions concerning the institution's pricing strategy, that is, the relation between tuition and financial aid, may be constrained by both competitive forces, such as the tuition of comparable, nearby institutions, and by economic forces, such as faculty salaries. Therefore, as part of the context for decision making, the board should understand both the opportunities and constraints that are placed on those decisions by the environment.

While the governing board needs to be aware of competitive forces, it is also important that it recognize the opportunities that exist for interinstitutional cooperation, particularly to the extent that such cooperation results in the sharing of resources or the avoidance of program duplication. In an environment characterized by increasingly scarce resources, it is essential that cooperation be as important a guiding principle as competition.

Suggested Questions

1. What are peer institutions or other institutions in the same geographic area doing about new programs, changes in tuition, and new methods of providing services (such as courses on weekends) that might significantly affect the ability of the institution to attract students?

2. How have the prices of major cost items changed—for example, faculty and staff salaries, library books, equipment, and energy—and what effect will those changes have on the institution's total budget?

3. Have there been any developments that would significantly affect the nature of the institution's traditional sources of revenue or the level of support they would provide—for example, the mood of the legislature regarding appropriations for education, feasible limits on student tuition, expected performance of investments, and gift projections?

4. Are students, at the national level, enrolling in the kinds of instructional programs offered by the institution? If not, in what kinds of programs are they enrolling?

5. What are the projected financial aid needs of the kinds of students who enroll in the institution?

6. Has any legislation, either state or federal, been proposed or passed recently that will have a significant effect on the institution? What are the financial implications of that legislation?

7. What steps is the institution taking to promote interinstitutional cooperation?

Chapter 2

Generating Financial Resources

Colleges and universities typically rely on a variety of sources for financial support. Students pay for the cost of tuition, room, and board; governmental agencies provide substantial subsidies and buy services; private sources make contributions and also buy services; the institution's own funds provide investment earnings; and the general public may pay for such services as patient care or for attending athletic events (see the accompanying table). Some revenue sources, such as the payment of tuition, can usually be used at the discretion of the institution, while others can be used only for purposes stated by the provider.

This diversity of financial resources requires a cohesive financing strategy and the development of administrative policies for providing management control in fulfillment of the institution's mission. The governing board has responsibility for approving the financing strategy and administrative policies.

The various revenue sources and their amounts are affected in part by the institution's mission, its form of governance, and its administrative policies. For example, publicly supported research universities rely heavily on appropriations from state legislatures and on federal grants and contracts, while a small, independent college derives most of its revenues primarily from tuition, private giving, and endowment earnings. Each institution's governing board should understand the limits of its various revenue sources. In addition, the board should be aware of the flexibility and degree of management control associated with each source of revenue.

This chapter examines each of the potential sources of funds listed in the accompanying table and describes the policy issues governing boards should consider. Chapter 5 describes the planning and budgeting concepts that can be used to blend the revenue sources into a financial strategy.

Source	Type of Revenue	Received Through
Students	Tuition and fees	Charge to consumer
	Room and board payments	Charge to consumer
Governmental sources (federal, state, and local)	Appropriations	Subsidy
	Grants and contracts	Reimbursement for services
Private sources	Gifts, grants, and contracts	Contribution or reimbursement for services
Institutional sources	Investment earnings	Investment of working capital and permanent funds
Sales and services	Educational activities	Charge to consumer
	Auxiliary enterprise activities	Charge to consumer

Students

To the student, total cost of attendance, rather than tuition or any other component, is the key figure. In setting the charge for tuition, room, board, and laboratory and student activity fees, the governing board should be aware that these must be determined in relation to each other. (Some residential colleges do have a comprehensive fee, but each component is nevertheless known to the board and administration.) The total amount billed and the rates of increase for each item are sensitive economic and political issues that governing boards must consider.

Tuition and Fee Rates

The tuition rate is established in a political environment; this needs to be understood by the board. Students, parents, alumni, faculty, taxpayers, and legislators have a vested interest in the tuition level. The governing board and administrative officers have the responsibility to explain the need for a tuition increase and to justify it in terms of academic program and economic considerations.

The board typically has the responsibility for approving tuition and fees, which are based on a combination of factors, including:

1. Balancing the budget. Tuition may depend on the amount needed to finance operating expenditures.

2. Historical precedence. Particularly in public institutions, there may be a political or historical basis for the relative tuition level. In this case, tuition for public institutions may be determined by the level of appropriations the legislature or other governmental body will provide.

3. Market conditions. A factor in determining the tuition rate is the amount charged by similar institutions. The governing board will want to be assured it is not *undercharging* or *overcharging* the tuition cost to students.

4. Relation to economic conditions. The annual increase in tuition may be tied to the rate of increase in personal disposable income or to an index measuring inflation. The rate of increase in tuition at independent institutions is generally related to the rate of increase in cost of instruction (salaries).

These factors impose the limits for increasing tuition. Public institutions may

Suggested Questions

experience larger tuition increases if legislative pressures, tax reductions, and/or inflation reduce relative governmental appropriations, but all colleges and universities face the pressures of additional inflation, new programs, regulatory requirements, and limitations on other financial resources, which tend to increase tuition or reduce services.

Activity fees are for special purposes, and are used to cover specific costs such as student health insurance and social and athletic programs. The amount assessed generally is directly related to the cost of the activity. (Room and board payments as sources of revenue are included in the section on sales and services.) Some fees collected by the institution are dedicated for purposes such as debt service; others are collected on behalf of student organizations.

In addition to tuition and fee rates as factors affecting the actual or net revenues from tuition and fees paid by students, there are two others: (1) student financial aid and (2) admission and retention rates. These are discussed below.

1. In public institutions, how does determination of the tuition rate relate to the appropriation process?

2. How does the total cost of attendance at this institution compare with costs of peer institutions?

3. How have increases in the total cost of attendance compared to increases in personal disposable income and inflation?

4. Is the institution relying more heavily on tuition as a percentage of total revenues?

5. Is there control over special-purpose activity fees?

Student Financial Aid

Financial aid to students can be in the form of grants (such as scholarships, fellowships, and tuition and fee waivers), employment, and loans. Such aid can be provided by governmental agencies, gifts from donors, institutional loan funds, or directly from unrestricted current funds (sometimes referred to as "unfunded financial aid"). Also, aid may be provided directly to the student and not administered by the institution, such as state aid programs for students attending institutions within that state.

One of the critical management issues facing academic institutions and of concern to governing boards is the funding of student financial aid. As tuition and room and board rates increase, so does the need for more financial aid. For example, when the board approves a tuition increase of $100, it should realize that a certain amount, say $25, will be needed to finance increased financial aid obligations. Only the remaining amount is available to meet inflationary pressures and the need for new programs.

The concept of financial aid being used to leverage tuition payments is not well understood. Stated simply, one segment of the student population pays the full tuition, another receives a subsidy (financial aid) that is paid from external sources such as governments and donors, and a third group (which typically overlaps the second) receives a discount financed from the institution's own funds.

Obviously, the relative size of each group has a significant effect on the tuition increase. For example, an institution having 80 percent of its financial aid provided by external sources, or by endowment funds restricted for scholarships, will benefit greatly from increased tuition rates, while an institution that provides 80 percent of its financial aid from its own funds will find it financially difficult to increase tuition rates and provide for the resulting financial aid needs.

In most cases, student financial aid is based on need. However, many institutions consider other factors such as academic achievement, vocational objectives, athletic ability, and leadership potential. Prudent allocation of financial aid also assists in developing the desired diversity of students and in maintenance of access to the institution.

Broad policies defining the objectives of the financial aid program should be recommended by the administration and approved by the governing board. These may be based on recommendations of a committee of representatives from academic departments, admissions and financial aid offices, student personnel office, business office, and student body. Such a financial aid committee should determine, in areas of its concern, standards and requirements relating to academic and other qualifications of applicants as well as methods used to evaluate their financial needs. The board should be aware of these standards and should approve the policies for administering financial aid.

Suggested Questions

1. What is the composition of the institution's financial aid by source and by type (grant, loan, employment)? How has the composition changed over time?

2. What is the relationship of financial aid requirements to a student budget (tuition, room and board, and other expenses)? How has this changed over time?

3. How do financial aid expenditures of peer institutions compare to those of this institution? How has this changed over time?

4. To what extent are the institution's unrestricted funds being used for financial aid? What is the percentage of tuition? What is the rate for peer institutions?

5. What is the distribution of financial aid by sex, ethnic origin, age, economic background, and how has this changed?

6. Are there possible changes in federal or state programs that will affect the availability of financial aid?

7. What percentage of students is receiving financial aid and how has this changed? (See Report No. 5, Part A, in Chapter 6.)

Admission and Retention Rates

The third factor affecting tuition and fee revenues is the institution's admission and retention rates. The admissions level is generally measured in terms of applications received, acceptances issued, and actual matriculation. For example, an institution may receive 1,600 applications, admit 1,000 prospective students, and have 500 students matriculate. The governing board should closely monitor these figures and relate them to those of previous years. Many public institutions having open admissions and extensive transfers may not be affected nearly as much by these factors for purposes of establishing tuition, but will be affected by the total number of students enrolled, compared with prior years.

In addition to examining the admissions figures, the governing board should be cognizant of the quality and diversity of the entering freshman class and how they compare with the quality and diversity of classes in prior years and with the institution's goals. Again, institutions having open enrollments may not be affected nearly as much by these factors. Board members should be aware of and should have approved the policy for admissions, which includes such factors as:

- Number of places available.
- Ratio of in-state to out-of-state admissions.
- Equality of access.
- Affirmative action.
- Admission criteria for entering freshmen, graduate students, and transfers.
- Level of academic admissibility.
- Evaluation criteria, such as high school grade average, class rank, test scores, and extracurricular activities.

The governing board should also be aware of how student preferences compare to the academic offerings of the institution and if there has been any noticeable change. In addition, the board should have an understanding of why students admitted to the institution but who declined acceptance chose another institution. The causes for not matriculating may point out weaknesses in the institution's academic offerings or other factors requiring examination.

The retention rate reflects the percentage of students remaining at the institution from year to year, and is another factor governing boards should examine (see Report No. 4 in Chapter 6). Significant changes in the retention rate may be due to changing student preferences, changing economic, political, or social conditions, or changing conditions on campus. In addition to having an effect on revenue, changing retention rates can be a signal for problems requiring administrative examination.

Suggested Questions

1. What are the application, acceptance, and matriculation figures for the entering freshman class, and how have they changed over time? (See Report No. 4 in Chapter 6.)

2. What is the mix (by ethnic origin, sex, class rank, family income, Scholastic Aptitude Test (SAT) score, etc.) of the entering class, and how has it changed over time?

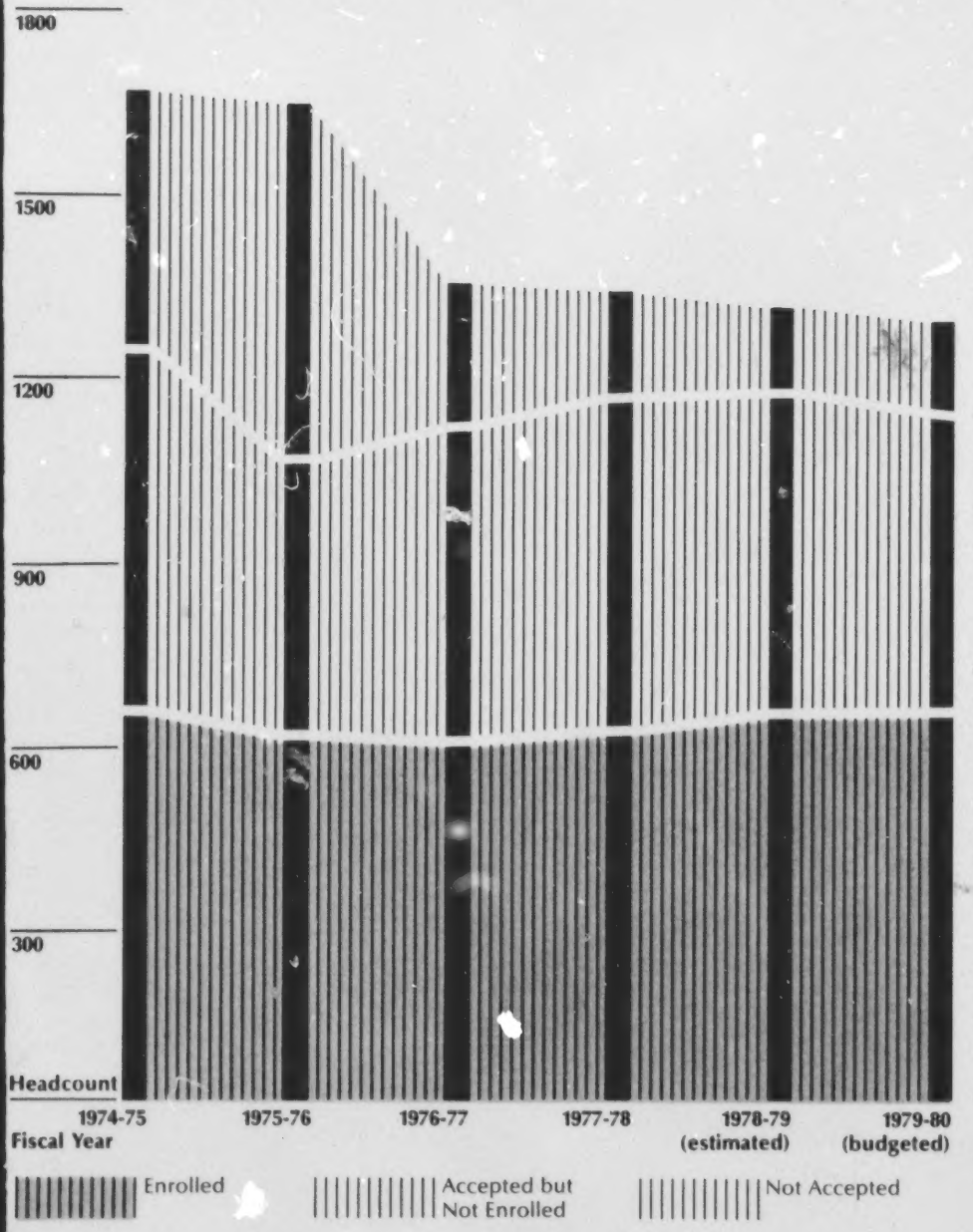
3. What are the reasons potential students have chosen other institutions, and how have these changed over time?

4. What are the institution's retention factors, and how have they changed over time? (See Report No. 4 in Chapter 6.)

5. What are the application, acceptance, and matriculation figures for transfer students by level and program, and how have they changed over time?

Student Application, Acceptance, and Enrollment

at Hybrid University



Governmental Sources

Each institution varies in its sources and levels of governmental support. The sources of such support can be classified as (1) appropriations (federal, state, and local) and (2) grants and contracts (federal, state, and local).

Appropriations

The appropriations process varies by jurisdiction and is related to requirements of the respective governmental authority. However, there are some basic reminders for every college or university.

First, the institution should have the expertise to communicate effectively with its respective governmental agencies. This expertise is in many forms, and effective communication requires persons who can express the institution's programmatic and financial needs.

Second, the institution should have an organizational structure that enhances its ability to communicate effectively with the agencies. Members of the governing board and designated institutional officers should be responsible for communicating directly to the agencies as required. Specifically for public institutions, the board must assume an advocacy role in presenting the institution's case to the legislature; this is one of its financial responsibilities.

Third, governing board members and officers of the institution should develop a spirit of cooperation with governmental authorities while at the same time maintaining the institution's autonomy. Often difficult to accomplish and to sustain, this effort requires sensitivity and understanding of the role and responsibility of the governmental authorities. The board should also have an understanding of the governmental authorities' priority for higher education and a sensitivity to the political environment.

Suggested Questions

1. Has the priority of higher education changed for the governmental authority? (This includes financial aid programs.)

2. What percentage of the governmental authority's budget is for higher education, and how has it changed over time?

3. How does the institution's governmental appropriation compare with appropriations for other similar institutions?

Grants and Contracts

An institution enters into grants and contracts when it is to the mutual benefit of the sponsor and the institution to undertake a specific work objective. In contrast to an appropriation, which typically is a funding authorization of a general nature, grants and contracts are generally legal arrangements that define a specific project to be conducted for a specific amount of money. Research projects, public service activities, institutes, and workshops are typical examples of this type of funding.

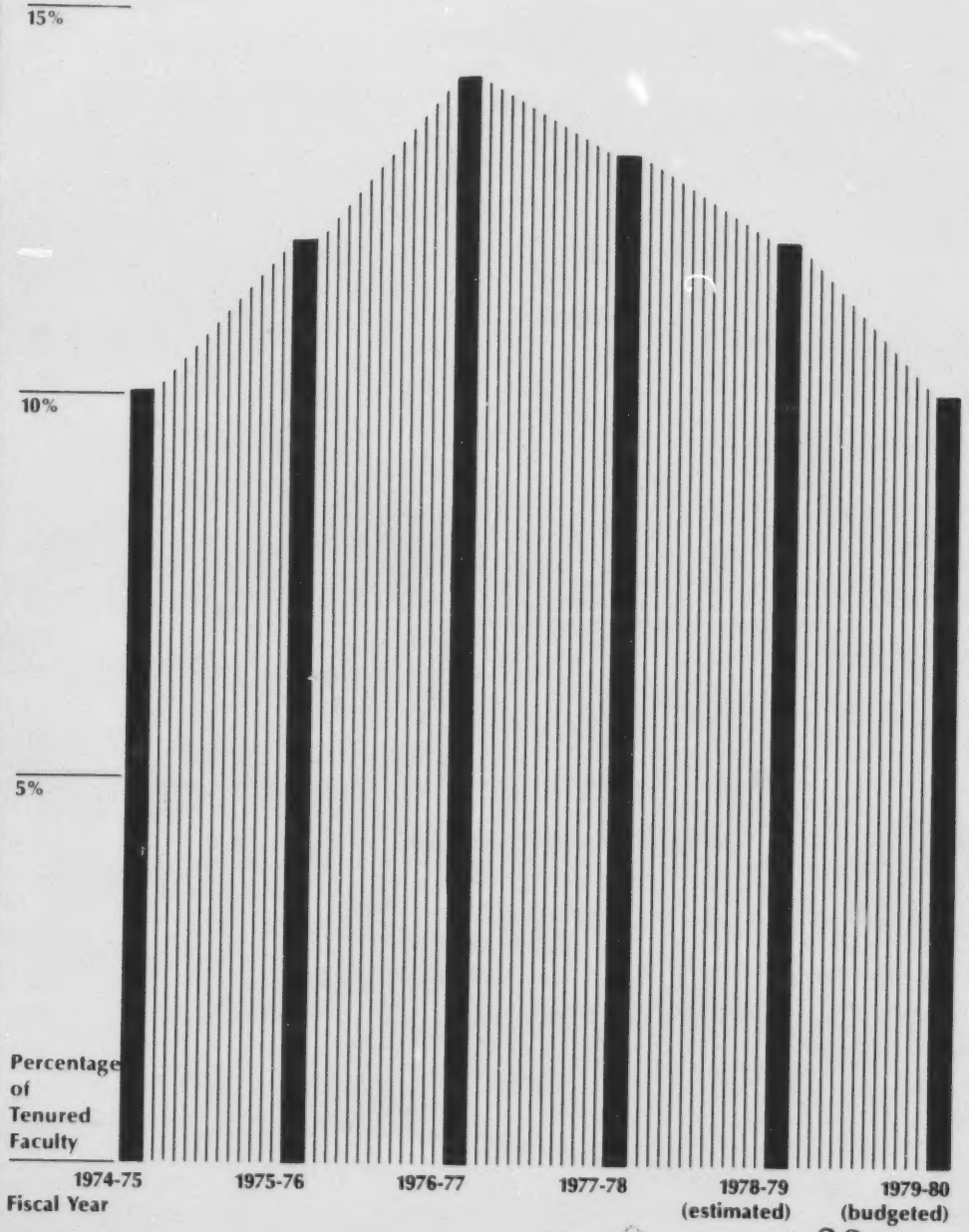
The governing board should help to establish and approve policies on grants and contracts, and the level of sponsored activity in relation to that of other activity should be reviewed by the board periodically. That is, the board should be aware of the institution's reliance on revenue from grants and contracts, and on a concentration of principal investigators, if such exists. Grants and contracts are generally of short duration (one to three years) and cannot be relied on to continue in the same sense as tuition or appropriations. The board should understand the consequences of major shifts in sources and interests of funding agencies on the total operations of the institution.

Although the revenue from grants and contracts increases total revenues to the institution, the additional accounting, recordkeeping, and reporting requirements of each funding agency must be considered, as they increase administrative and support costs. Federal grants and contracts are subject to changes in the method of reimbursing indirect costs. This has been and continues to be a major problem between universities and the government; it stems primarily from the fact that joint products (teaching and research) are involved. Because they are so intertwined, calculation of the indirect cost rate is a complex procedure.

Federal grants and contracts are also forces for social progress, as their provisions regulate employment and other practices. Colleges and universities are "employers" and many are "federal contractors," with the responsibilities that these terms carry. Thus, in accepting grants and contracts, institutions also accept their provisions such as (1) special reporting of policies and practices for patents and copyrights, and (2) promoting equity in employment, advancement, admissions, and other areas.

Percentage of Tenured Faculty Paid from Grants and Contracts

at Hybrid University



Suggested Questions

1. Does the institution have adequate policies with regard to personnel administration, patents, copyrights, and rights of privacy to comply with legal obligations accepted under certain grants and contracts?

2. Does the institution have a stated policy on the kinds of research and public service activities to be undertaken and funded by grants and contracts?

3. To what extent are salaries of tenured faculty being funded from grants and contracts?

4. What is the outlook for the future funding of grants and contracts?

5. What is the institution's reimbursed indirect cost rate and how has it changed over time? What is the actual cost to the institution?

6. How has the institution fared with government audits?

7. Is the institution responding in a timely fashion to proposed federal regulations?

8. To what extent are funding agencies fully reimbursing direct and indirect costs incurred on their projects?

9. Is the institution responding to opportunities for acquiring grants and contracts?

28

Private Sources

Monies received by colleges and universities from private sources are from either charitable contributions or grants and contracts. Charitable contributions are usually received as a result of solicitation by members of the governing board, certain administrators, professional staff, and alumni volunteers. Grants and contracts entered into with private sources are generally initiated by the faculty, although some of these may be the result of fund raising by professional staff.

Traditionally, independent institutions have emphasized the raising of funds from private sources, but rising costs have forced more public institutions into fund-raising activities. Conversely, economic factors have forced independent institutions to apply to the state for funds (principally, capital and student financial aid).

The governing board should have a thorough understanding of the relative importance of funds received from private sources and, when needed, should become actively involved in solicitation. The more reliant an institution is on gifts, the more attention should be devoted to fund raising, policy formulation, long-range planning, and review of performance.

The governing board should approve policies governing the kinds of gifts that can be accepted, and such a policy should also include criteria for rejecting gifts, such as those having unacceptable or illegal restrictions or those whose costs of administration would be excessive. It should also have an understanding of the institution's fund-raising strategy and goals. Monies from private sources can come from board members, alumni, friends, corporations, and foundations (see Report No. 8 in Chapter 6). Gifts can be in many forms, including pledges, bequests, and annuity and life income funds. They can be annual, ongoing gifts as well as large, one-time capital gifts.

The various forms of giving are affected differently by economic conditions, tax laws, social-political influences, and the institution's fund-raising efforts. For example, large capital gifts are influenced by stock market conditions, whereas corporate giving is more strongly influenced by pretax profits. Board members should be aware of the different kinds of support received from private sources and should have a basic understanding of how that support can be affected by varying conditions.

Suggested Questions

1. Does the institution have a policy describing the kinds of support it can accept from private sources?

2. How has support from private sources changed over time? Has it kept pace with inflation? How has it compared with other revenue sources? What are the prospects for the future? (See Report No. 8 in Chapter 6.)

3. How is support from private sources being used? Are there certain programs heavily reliant on the receipt of gifts and grants?

4. How do the institution's fund-raising activities compare with those of peer institutions?

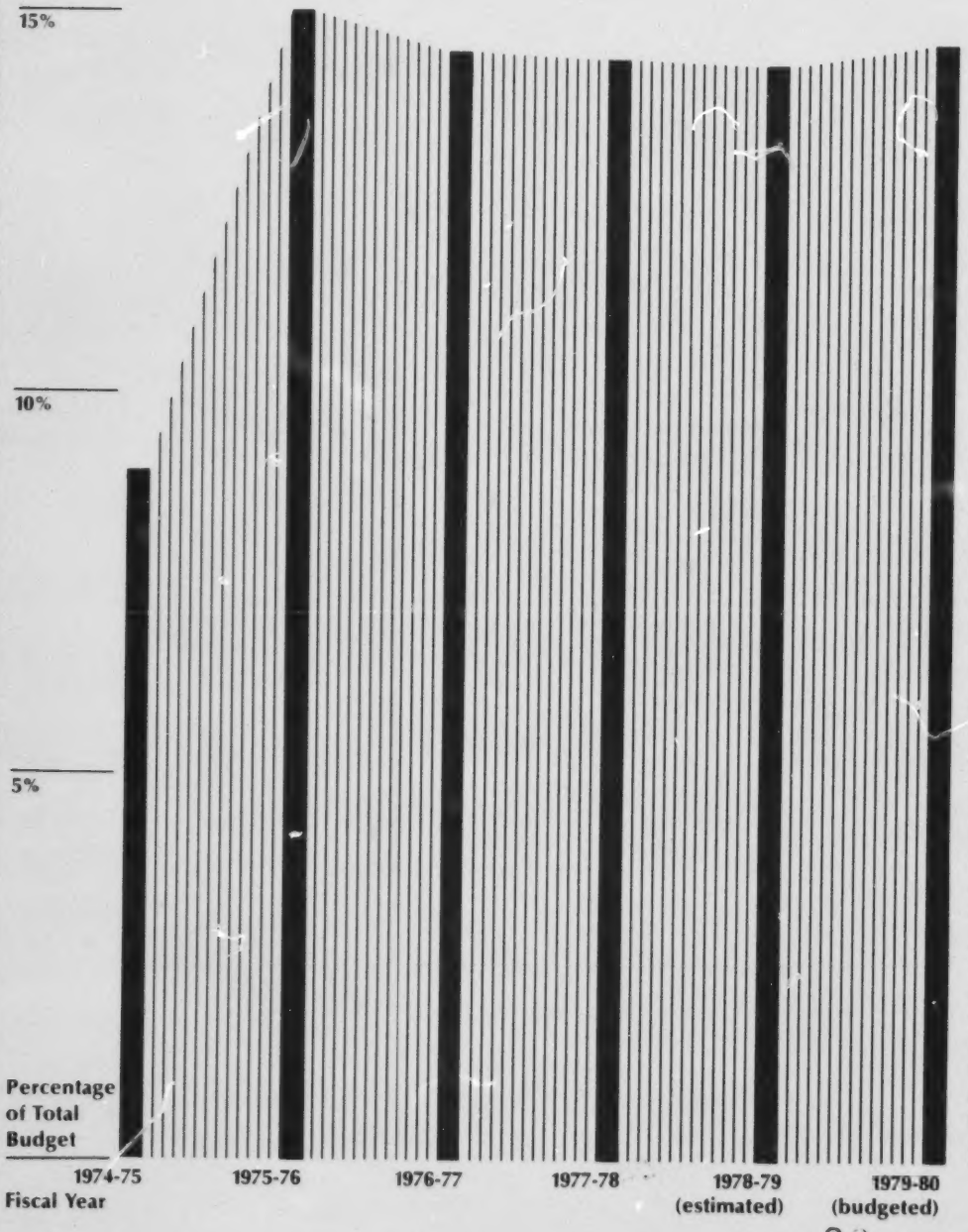
5. Are there anticipated economic regulations and/or social-political changes contemplated that will affect revenues from private sources?

6. What is the overall strategy for raising revenues from private sources? Is there need for a major fund-raising campaign?

7. What effects will anticipated changes in tax laws have on gift-giving? Is the institution doing anything about them, such as communicating its concern to legislators?

Gifts Used in Operating Budget

as a Percentage of Total Budget at Hybrid University



Institutional Sources

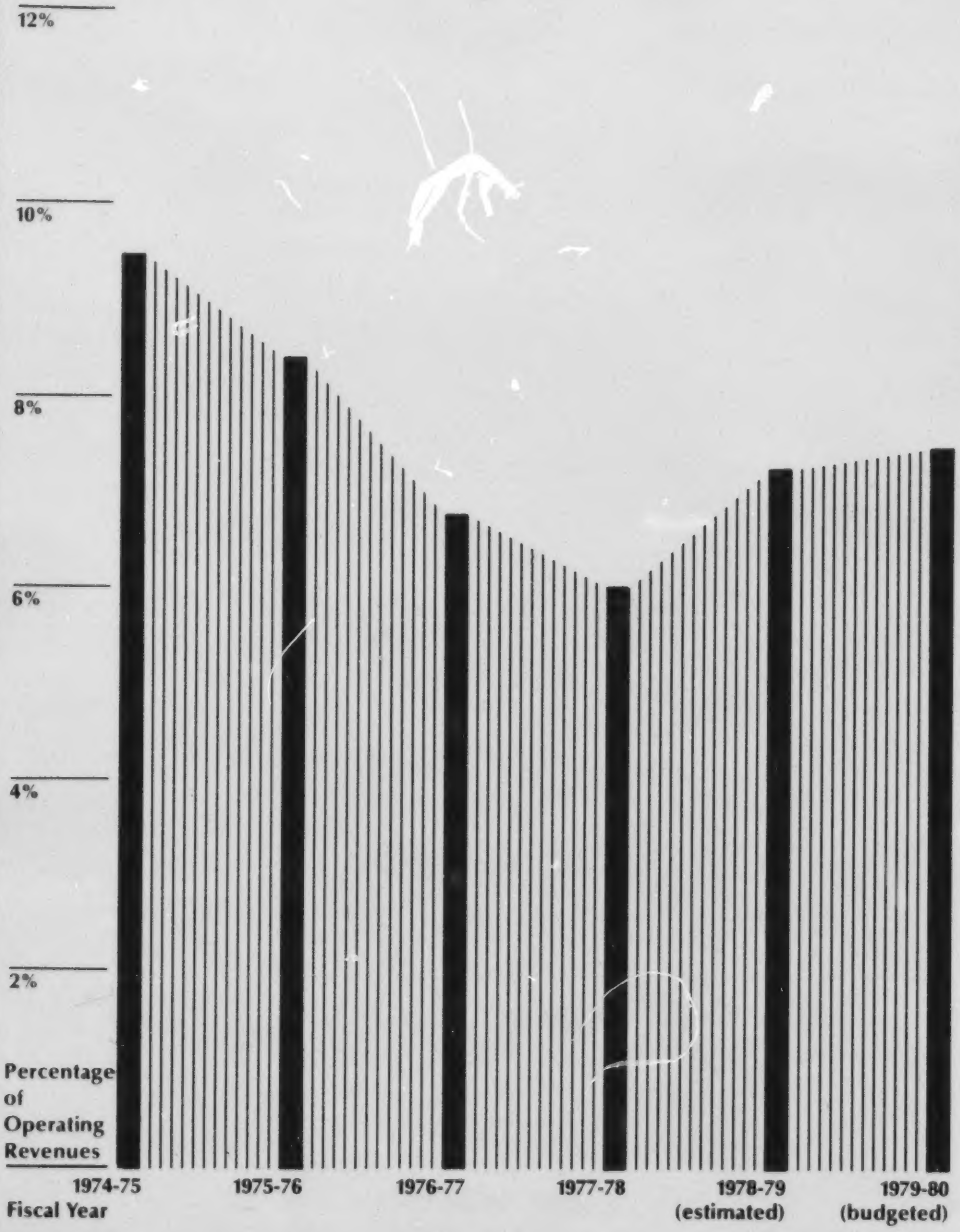
Investment earnings are generated by the various "fund groups" of the institution, including current, loan, endowment and similar, life income and annuity, and plant. The current, or operating, fund would generally be invested for the short term, while the other funds typically would be invested for longer periods. Use of the earnings may be restricted or unrestricted; for example, earnings of restricted student loan funds may be used only for student loans.

The cash flow requirements, risk levels, restrictions on investment, and investment objectives vary for each kind of financial resource. Since the governing board has stewardship responsibility for all resources, members should have an understanding of the kinds of financial resources available for investment and should approve policies establishing objectives for investment and its management. Institutions with large endowments must devote much time and money to actively investing their endowment portfolio.

When determining investment objectives, the governing board should have an understanding of such economic factors as inflation, interest rates, and the national economy, as these affect performance. The board has responsibility for the appointment of investment managers and may delegate full discretionary powers to the managers, or the institution itself may handle the investments. The board should also approve, for each type of fund being invested, the expected investment objectives, desired level of risk, term of investment, portfolio mix, and investment performance. Whatever method of managing investments is adopted, the board has the responsibility for investment performance.

Endowment Earnings Used in Operating Budget

as a Percentage of Operating Revenues at Hybrid University



Suggested Questions

1. Does the institution have investment policies that cover all of its financial resources?

2. Have investment performance objectives been established? Do they consider such factors as existing and forecasted economic conditions, anticipated payout rates, preservation of endowment purchasing power, acceptable level of risk, and portfolio mix? Should the total return concept be adopted (for spending levels)?

3. Do the investment managers have a clear understanding of their authority and responsibility?

4. Has investment performance met expectations? How does performance compare with that of peer institutions and with nationally recognized indexes over an extended period?

5. Does the investment policy describe the institution's social responsibility with regard to investments?

Sales and Services

Revenues from sales and services can cover a broad range of activities. Some of these are:

Sales and Services of Educational Activities

- Film rentals
- Testing services
- Home economics cafeteria
- Demonstration schools
- Dairy creameries
- College theaters

Sales and Services of Auxiliary Enterprises

- Residence halls
- Faculty housing
- Food services
- College unions
- College stores
- Intercollegiate athletics

Sales and Services of Hospitals

- Daily patient services
- Nursing services
- Other professional services
- Outpatient services

Services provided by such activities assist in creating the educational environment, and in some instances are a required ingredient in the educational process. These activities generally are operated like businesses, each having financial plans and budgets reflecting revenues and expenditures. Sales and services activities generally are maintained under the same budgetary controls as academic and administrative departments, with some institutions setting aside reserves for depreciation or replacement. The governing board should be aware of the purpose and extent of the institution's sales and services activities and be assured that the activities are necessary and beneficial to the institution's mission.

In some cases, such as residence halls, food services, and hospital services, a correlation may be sought between the cost of the service and the price charged, including depreciation and indirect costs. However, other activities may charge a price that is subsidized from other funds. The governing board should approve the pricing policies for these types of activities, determining to what extent, if any, they should be subsidized. In addition, boards should be aware to what extent any of these activities may be considered as unrelated businesses, and thus subject to reporting for federal income tax purposes.

Some services may be contracted to third parties having expertise and management skills not to be found in the institution. Whether managed internally or externally, the board should determine that they are being managed in an efficient manner.

Suggested Questions

1. Does the institution have policies documenting the purpose of its sales and services activities?

2. Are there policies establishing the criteria for pricing sales and services activities?

3. To what extent are the institution's unrestricted funds being used to subsidize sales and services activities? How has the subsidy changed over time?

4. Are the prices being charged competitive with those of other suppliers, if any?

5. Has the possibility of using contract services been explored?

6. Have the costs been reviewed to determine if they were fully allocated?

Chapter 3

Spending Financial Resources

The financial resources used by colleges and universities are intended to provide services to society. They are held in trust by the governing board and should be managed prudently and effectively in accordance with the institution's mission. This is a difficult responsibility because there is no single set of generally accepted guidelines for allocating these resources.

This chapter describes policies that will assist the board in overseeing the best use of the resources entrusted to it. The financial planning and budgeting processes discussed in Chapter 5 provide a systematic analysis of the institution's programs and result in resource allocation across programs and across time. The budget is not only a control document, but also gives further definition to programs.

How financial resources are spent can be examined from several perspectives. Some of the more common classifications of expenditure are:

By function	By organization	By object
Instruction	College	Personnel compensation
Research	School	Supplies and expenses
Public service	Department	Capital expenditures
Academic support	President's office	Buildings
Student services	Vice presidents' offices	Equipment
Institutional support	Etc.	Library resources
Operation and maintenance of plant		
Scholarships and fellowships		
Auxiliary enterprises		

In the planning and budgeting process (see Chapter 5), the *functional* classification of expenditures is used to identify and evaluate the institution's programs, while the *organizational* classification of expenditures is necessary for operational control and establishing budgetary authority. Classification by *object* of expenditure is useful for determining and establishing administrative policies, and is the one used in this chapter, which discusses several issues requiring policy formulation. All the issues (and any others that could be named) are related to the major object-of-expenditure categories listed in the table above. The issues selected here are faculty and staff, purchasing, maintenance and replacement of capital assets, and energy.

Faculty and Staff

Financial policy issues concerning faculty and staff generally involve at least the following: salaries, benefits, employee relations, equal opportunity and affirmative action, faculty effort, and conflict of interest.

Salaries

Because salaries are such a large portion of the institution's operating costs, as much as 75 percent, governing boards should have an understanding of the policies used to administer those expenditures. Salary policies can be complex due to the broad range of types of employees. This diverse range includes:

Faculty
Tenured (and by rank)
Nontenured (and by rank)
Temporary or part-time
Adjunct
Teaching and research assistants

Staff
Salaried full-time
Hourly full-time
Student
Casual

The governing board should have an understanding of the trends of faculty and staff salary levels. Two trend indicators are the change in number of students in relation to number of faculty and the change in number of administrative/support staff in relation to the number of faculty. Significant variation indicates a change in operations, of which the board should be aware. Policies relating to salaries will help insure that salary levels are determined in a rational, well-documented manner and in accordance with existing legislative, union, and regulatory requirements. Salary policies should include procedures for reviewing performance and determining salary increases.

A related issue affecting the amount paid is faculty tenure. Although tenure is normally considered in terms of academic issues, it also carries significant financial implications. The governing board should be aware that as the percentage of tenured faculty increases, the institution assumes increasing long-term financial and program commitments, diminished financial and employment flexibility, and higher faculty salary levels. Thus, the board should review and approve a tenure policy, which includes:

- Terms of academic appointment.
- Process of and criteria for granting tenure, if applicable.
- Criteria for notice of dismissal.

Another area of concern to the governing board is competitiveness of the institution's salaries. Through the exchange of salary information with peer institutions and the use of national, state, and regional wage and salary surveys, the board should be kept informed of the institution's relative salary levels.

Suggested Questions

1. Has the governing board reviewed and approved a statement of the different types of faculty and staff categories?

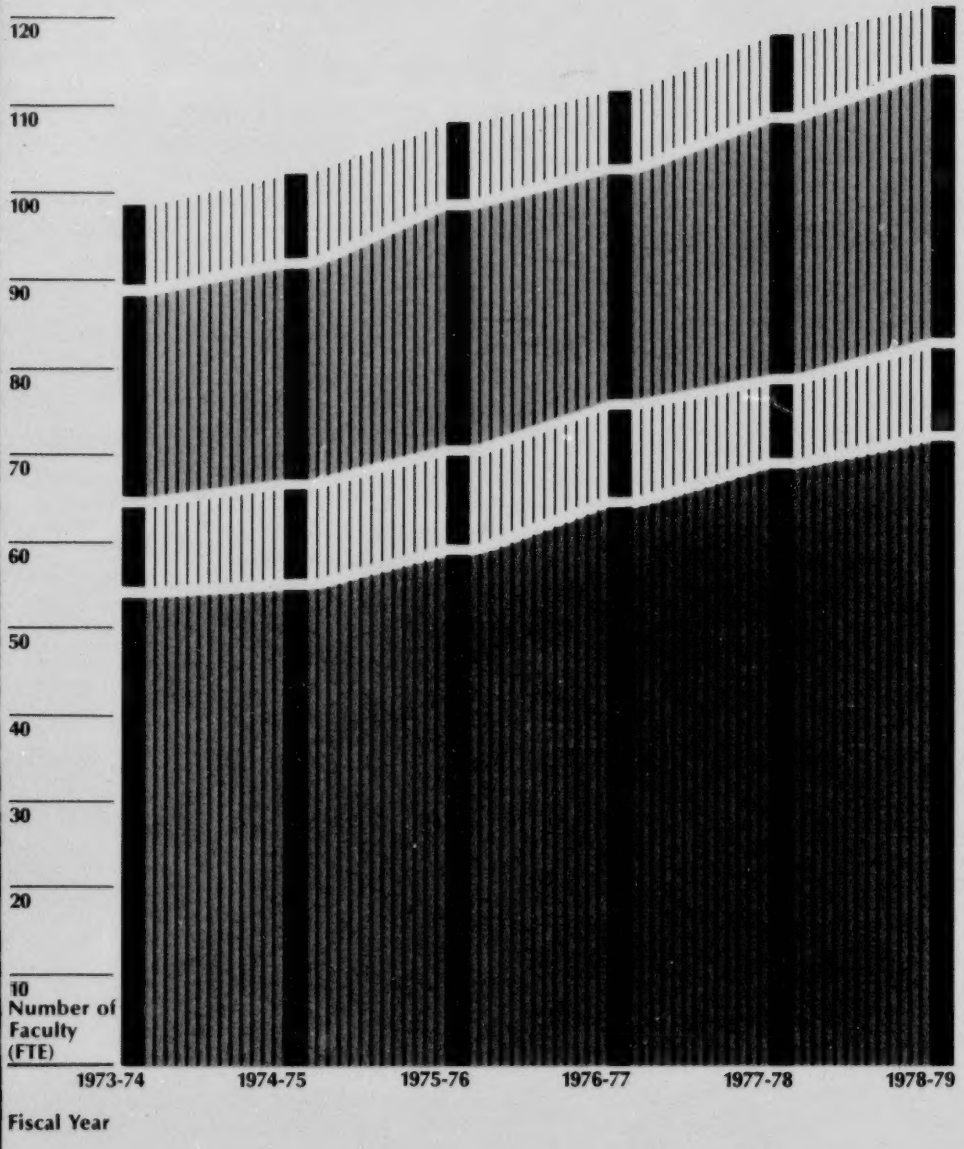
2. Does the institution have a stated tenure policy? If so, how does it compare with other statements on tenure?

3. What have been average faculty and staff salary levels in recent years? How does the growth of the institution's faculty salaries compare with the growth of those in peer institutions, with the consumer price index, and relevant market salary surveys?

4. What is the history of faculty turnover?

Number of Faculty by Rank

for Hybrid University



Benefits

Faculty and staff benefits are a significant part of total compensation, and can include the following:

- Medical care
- Short- and long-term disability income
- Life insurance
- Accidental death insurance
- Travel accident insurance
- Retirement and social security
- Sick time
- Vacation time
- Sabbatical and other leave
- Tuition remission

This is not an exhaustive list, and in some institutions additional benefits may be offered; also, within each benefit category a variety of options is available. Benefits can be granted to employees with the full cost being absorbed by the institution, or the cost may be shared by agreement between the employee and the institution. Furthermore, certain benefits may be offered to some classes of employees and not to others.

Employee benefits may be 30 percent or more of salaries and may affect salary levels, recruiting and hiring, and union negotiations. Individual benefit options should be managed and evaluated within the context of the overall objectives of the benefits program. The policy should include evaluation of trade-offs among individual benefits and procedures for cost control over the total benefits program.

Suggested Questions

1. What is the basic objective of the benefits program? What general principle should guide how the costs are to be divided between the institution and the employee?

2. Does the policy include criteria for employee eligibility?

3. Has a procedure been established for periodic review of the cost of individual benefit programs?

4. Is there the potential of changing legislation that could affect benefit programs and their costs?

5. How do quality and cost of the benefit programs compare with those of peer institutions?

Employee Relations

The governing board should review and approve employee relations policies. The following may be included:

- Recruiting and hiring policies
- Grievance procedures
- Seniority
- Holiday, vacation, and sick leave
- Leaves of absence
- Performance reviews

Federal, state, and local laws prescribe policy in some of these areas, but stated policies are required in all of them to define the rights of the institution and those of the employee.

Another issue facing institutions and their governing boards relates to recognition of and negotiations with labor unions. The board should be aware of and should have approved the position the institution has taken with regard to unionization; unfortunately, many boards wait until bargaining units have been formed at their campuses before addressing collective bargaining issues. If the institution has an agreement with a union, the board should review strategy regarding negotiations and should be kept informed of the institution's union relations.

Suggested Questions

1. Does the institution have administrative policies for recruiting and hiring, grievance procedures, seniority, vacations and holidays, and leaves of absence?

2. What is the institution's position on unionization of its employees?

3. If there is an existing union agreement, what is the status of union relations? If not, are unions seeking to organize?

4. How effectively has the institution's administration negotiated the existing agreement(s)?

5. What has been the effect of collective bargaining on the institution's operations?

6. Is there opportunity for employee participation in planning benefit programs?

Suggested Questions

1. Does the institution have an established equal opportunity policy?

2. Has the institution complied with federal and state regulations governing equal opportunity?

3. Has there been improvement in the relative position of minority group members and women in the institution's faculty and staff? How has performance compared with expectations?

Equal Opportunity and Affirmative Action

Federal regulations and the institution's own commitment to fair practices make it imperative that programs be developed to provide equal opportunity to all persons regardless of race, color, religion, sex, age, physical or mental handicap, or national origin. The effective pursuit of equal opportunity requires not only the adoption of a formal policy, but also results-oriented procedures that insure the involvement of managers at all levels.

The policy, which should be reviewed periodically, should document the principles and organization for conducting the equal opportunity program; it should conform to all existing legislation and regulations, reflecting the spirit of equal opportunity in education and employment. A strong affirmative action program will probably result in increased costs. Additional recordkeeping, supervisory training, and administrative effort are examples of activities that contribute to increasing costs.

Suggested Questions

1. Does the institution have a policy on faculty effort describing standard teaching loads, released time available for research, administrative requirements, etc.?

2. Has the board established policies governing consulting activities of its faculty and determined if they are consistent with academic program objectives?

Faculty Effort

A recurring subject is how faculty members should spend their time. The reason this subject is never settled is that teaching, counseling of students, committee work, research, and public service endeavors of the faculty are virtually impossible to quantify. However, there are several policy factors regarding faculty effort that are of concern to governing boards. The need for a policy on faculty effort is important because of its effect on faculty employment and retention, institutional finances, and educational quality.

There should be a policy that defines standard full-time teaching loads; released time available for research; guidelines for outside consulting; and the time requirements for student counseling, administration, committees, and other functions. The policy should be designed as a broad framework in which the president and academic officers have the flexibility to make faculty assignments within a wide discretionary range.

Conflict of Interest

A conflict of interest exists when a board member, officer, or other key person may have an outside interest that has the *potential* of being at variance with the best interests of the institution, even though that interest may not, in fact, be financially detrimental to the institution. Examples include:

- Conflicting personal financial interests (doing business with the institution).
- Use of confidential information for personal gain.
- Unauthorized disclosures of confidential information.
- Gratuities.
- Outside employment.
- Use of institutional time and facilities for personal purposes and other activities.
- Contributions in kind.

The conflict-of-interest policy should be designed to provide board members, officers, faculty members, and staff with guidelines that can be followed when they engage in activities that may conflict with the institution's interest. Just the appearance of conflict of interest, when in fact it may not exist, can be damaging to the institution. Therefore, a policy of disclosure is necessary, and forms have been developed for this purpose

Following are two possible options for the purpose of developing and maintaining adequate records. Either option can be modified or adapted, with advice of legal counsel, to institutional circumstances and board judgment. Neither form is presented as a perfect device. Boards electing to adopt a version of either form are urged to require each board member to complete and update it annually. Further, the forms should be formally reviewed on a schedule and by an official or officials determined by the board.

For a complete set of guidelines on conflict of interest, see "Guidelines for Policies Affecting Potential Conflicts of Interest," which is available from the Association of Governing Boards. The two forms below are included in that publication.

OPTION I: CONFLICT OF INTEREST QUESTIONNAIRE

_____
(Institution Name)

_____
(Name) (Date)

_____
Office Held (Trustee, Vice President for Administration, etc.)

1. Are you an officer or director of any corporation with which _____(institution name)_____ has business dealings? Yes _____ No _____
If the answer to the foregoing question is "yes," please list the names of such corporations, the office held, and the approximate dollar-amount of business involved with the (college or university) last year.

_____
_____
_____
_____

2. Do you, or does any member of your family, have a financial interest in, or receive any remuneration or income from, any business organization with which _____(institution name)_____ has business dealings? Yes _____ No _____
If the answer to the foregoing question is "yes," please supply the following information:

a. Names of the business organizations in which such interest is held and the person(s) by whom such interest is held:

_____
_____
_____
_____

b. Nature and amount of each such financial interest, remuneration, or income:

_____
_____
_____
_____

3. Did you or any member of your family receive, during the past twelve months, any gifts or loans from any source from which _____(institution name)_____ buys goods or services or with which _____(institution name)_____ has significant business dealings? Yes _____ No _____
If the answer to the foregoing question is "yes," list such gifts or loans as follows:

Name of Source	**Item**	**Approximate Value**

I certify that the foregoing information is true and complete to the best of my knowledge.

_____
Signature Date

OPTION II: DISCLOSURE LETTER

Board Secretary (or other designated official)
(Name and address of college or university)

Dear _____:

I have received and read the statement of "Policy on Conflicts of Interest" approved by the board on __(date)__, and I am in compliance with the policy except as specifically set forth below.

For the information of the (college or university), I am listing on the reverse all of my "associates" as defined, and the position and/or interest which I or members of my family have in each "associate."

Sincerely,

_____

Signature Date

Exceptions
(Note: If there are none, please write "None.")

Associates*

Trustee or Family Member**	**Associate**	**Position and/or Interest**

*An associate of an individual includes any person, trust, organization, or enterprise (of a business nature or otherwise) with respect to which the individual or any member of his or her family (1) is a director, officer, employee, member, partner, or trustee, or (2) has financial interest as described in the board's policy on conflict of interest adopted on (date), or any other interest which enables him or her to exercise control or significantly influence policy.

**The family of an individual includes his or her spouse, parents, siblings, children, and any other blood relative.

Suggested Questions

1. Does the institution have a conflict-of-interest policy that clearly states guidelines to be followed? Does it require disclosure by board members and administrative officers of activities related to their responsibilities?

2. Has the institution experienced conflict-of-interest situations? If so, could they have been avoided with an effective policy?

Purchasing

An effective organization for purchasing promotes the institution's objectives by providing faculty and staff with necessary supplies, equipment, and services. Purchasing is centralized at most colleges and universities, and has as its objective to identify, select, and acquire needed materials and services as economically as possible within accepted standards of quality and service. In such a system, authorized persons within departments initiate purchase requests that are forwarded to the purchasing department, which in turn issues the purchase order.

Many independent colleges and universities have cooperative purchasing arrangements, resulting in lower overhead and lower prices. Purchasing procedures at public institutions usually conform to the requirements of state law. Terms of federal and state grants and contracts often stipulate the use of specific purchasing procedures and levels of documentation.

A policy statement on purchasing should include those external requirements, responsibilities of the purchasing department and assignment of authority within the department, criteria for selecting vendors, and bidding procedures, including sole-source approval. It should also consider the special requirements for library books, periodicals, computer hardware, and scientific and medical equipment, as well as provisions for considering lease/buy decisions that arise with such items as computers, copying machines, and typewriters. Policies for evaluating contracted services of auxiliary enterprises and certain physical plant functions should also be included.

Suggested Questions

1. Does the institution have a purchasing policy that clearly defines responsibilities, organization, and criteria for purchasing?

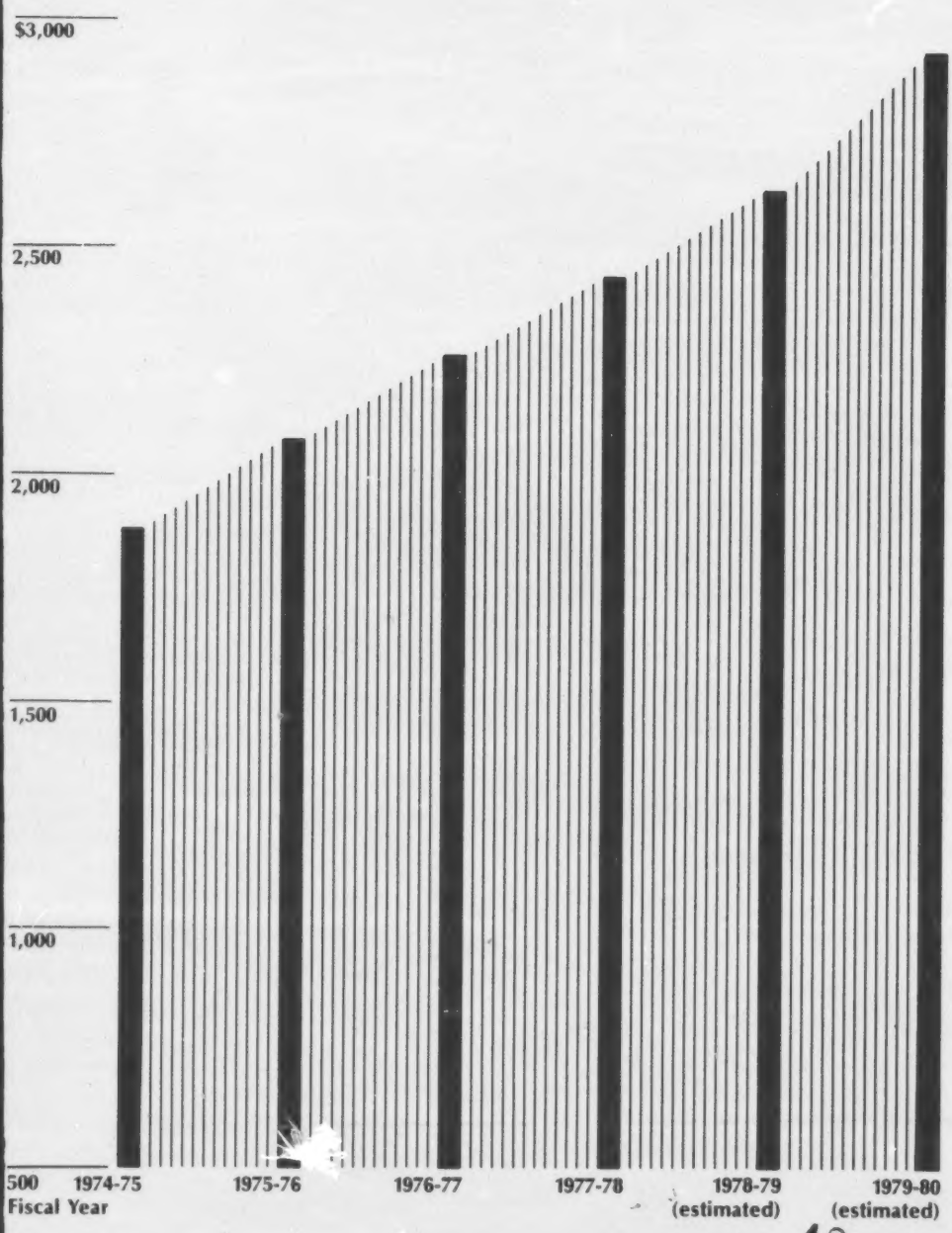
2. Does the institution have a policy of periodically auditing the purchasing function? Have there been any significant findings requiring administrative action or review of the purchasing policy?

3. What special policies have been established for the purchase of library books, computers, and medical equipment and supplies?

4. Are there other organizations that can be joined for cost-effective joint purchasing arrangements?

Estimate of Neglected Maintenance Cost

(Cumulative) at Hybrid University
(in thousands of dollars)



Maintenance and Replacement of Capital Assets

The governing board has ultimate responsibility for protecting the institution's physical assets. Members should understand the process of identifying maintenance and replacement projects, establishing priorities, and evaluating the sequence of projects to be performed. They should also be assured of the institution's compliance with local, state, and federal requirements regarding health and safety conditions and access for the handicapped.

Many colleges and universities have neglected maintenance in order to balance budgets or to decrease deficits. Such a practice may be unavoidable, but it may lead to extensive future funding requirements for maintenance that will have to be paid ultimately by future generations of students, taxpayers, and donors. Therefore, in addition to reviewing major maintenance and replacement projects, the board should review the institution's preventive maintenance policies and should know how much maintenance is being deferred and what the consequences of such deferral are.

Governing boards must also consider plant expansion, new construction, and replacement and major renovation of existing facilities. The rising cost of construction, coupled with scarcity of funds, has placed many institutions in the position of not expanding, maintaining, or replacing plant as required. Some institutions have used debt financing or unrestricted gifts for capital improvements.

Depreciation is sometimes discussed in the erroneous context of replacing capital assets. There is a misunderstanding on the part of many who have felt that if colleges and universities had recorded an amount for

depreciation in their financial records, then funds would have accumulated that would have been available for replacement and major renovation of facilities. However, what is overlooked is that to accumulate a reserve, an institution would have had to use such means as higher tuition and unrestricted gifts otherwise available for current program needs.

The approach for replacing capital assets is different for public and independent institutions. Most public institutions will probably continue to rely on the capital appropriation process and to justify their requests on a pay-as-you-go basis. The problem is markedly different for independent institutions: there is no readily identifiable source of funds for renewals and replacements; donors and the federal government have shown less interest in financing these kinds of projects. Some states have agencies that will obtain funds for independent institutions for the construction or renovation of facilities at low rates of interest, but the annual debt service may be in excess of available funds from operations. As a result, governing boards of independent institutions may wish to consider the need for a recurring charge to be included in the operating budget that will accumulate a reserve to be used for renewals and replacements.

If an institution does not have a capital appropriation procedure with a governmental agency, the board should review and approve a policy defining a systematic method for financing the renewal and replacement of capital assets. The policy statement should include provisions for periodically evaluating the condition of facilities and for reexamining the estimated reserve requirement.

Suggested Questions

1. Does the institution have a systematic approach to the maintenance of facilities?

2. What criteria are used for budgeting maintenance expenditures?

3. To what extent, if any, has maintenance been deferred?

4. Does the institution have a plan and schedule for determining the financing of replacement and renovation of facilities?

5. If there is not a capital budget appropriation process, is there an adequate flow of revenues being set aside to replace and renovate the facilities?

Energy

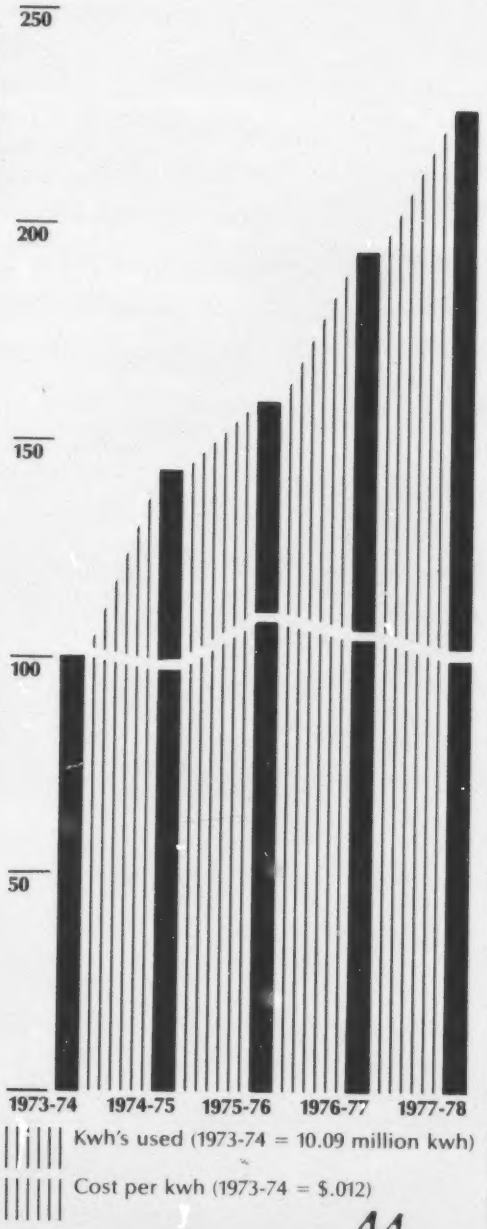
Energy is the most rapidly growing expense item for most colleges and universities. The governing board should be aware of the energy issues at its institution and should see that an energy program has been adopted; such a program should be developed by the administration. The program can cover energy use limitations for future building construction, an energy conservation program, establishment of an ongoing energy office, and criteria for determining energy-saving conversion projects.

Suggested Questions

1. Does the institution have an energy management program?
2. What energy-saving measures have been taken and how cost-effective have they been?

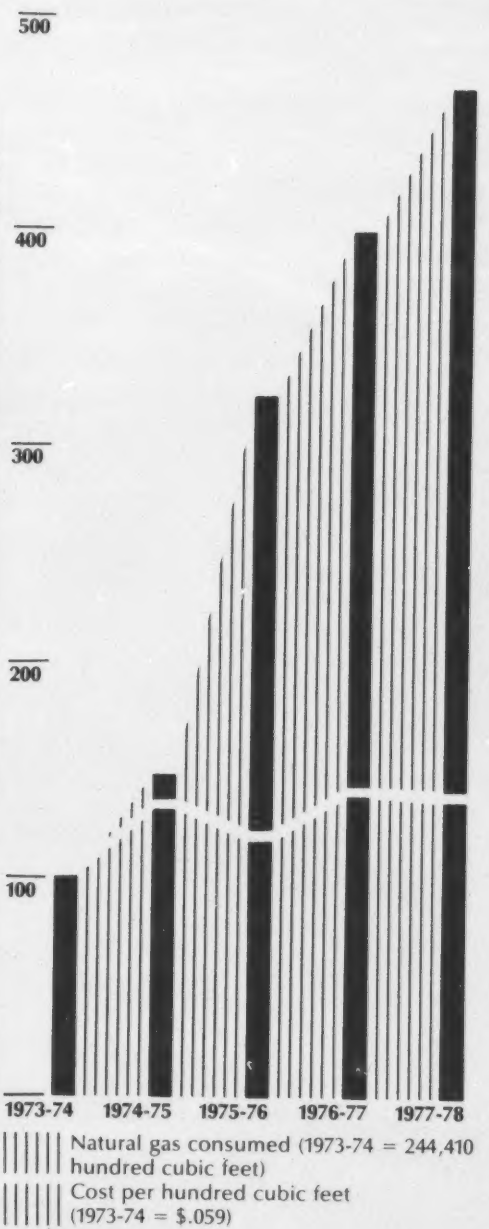
Electricity Use and Cost

for Hybrid University
(1973-74 = 100)



Natural Gas Consumption and Cost

for Hybrid University
(1973-74 = 100)



Chapter 4

Managing and Protecting Financial Resources

The financial reports of a college or university present a picture of resource flows in dollar amounts over a particular period and the resulting balances for the future. Chapters 2 and 3 discussed the generation and spending of resources; this chapter is concerned with what balances remain and for what purposes, and with measuring their adequacy in fulfilling the institution's mission.

Financial reports of colleges and universities suffer from some of the same deficiencies as those of business entities. Balance sheet figures can never adequately measure the wealth of knowledge, experience, and potential inherent in faculties, student bodies, administrators, governing boards, and other supporters. Inflation and the never-ending pressures on educational institutions for "more"even call to question evaluations of such traditionally measurable assets as marketable securities and real estate. The board must be concerned with both adequacy and stability of the institution's capital base.

It is unfortunate that typical reports from an accounting system especially designed to insure proper stewardship of resources in nonprofit institutions should appear confusing and unhelpful to the stewards. Would "resource accounting" be a better term than "fund accounting"? (See the last section of this chapter, "Guide to Fund Accounting.") As businesses are asked to provide more disclosure and accountability, they may be moving more toward fund accounting than is recognized; and as nonprofit institutions are challenged to become more "businesslike," they may be accepting more of the traditional, for-profit business accounting than they appreciate.

Businesses range from the simple to the complex; so do educational institutions, and so do their financial reports. In order to know how the financial resources of the institution have been managed and protected, members of the governing board should be able to read

the financial statements or to obtain an adequate understanding of them from management or auditors. The significant decisions of resource allocation among competing needs today, and between today and tomorrow, require an appreciation of the resources available and of those that will become available in the future. Where are they? What are they? How can they be used most efficiently and effectively? When and where are more needed?

The financial statements of a college or university could be regarded as those of a "conglomerate," in which the separate parts appear to be given more attention than the whole. The governing board must recognize both the parts and the totality, and appreciate the differences. In pursuit of its goals, an educational institution performs teaching and research in its current operations, runs a loan "business" to help finance its "customers," maintains an investment facility for itself and others of interest, operates a physical plant, and may even manage specialized stores, dining rooms, housing and other commercial-type enterprises, and hospitals in serving its constituency.

Because it depends on supporters who have varied interests among these activities, a college or university must keep its books more in accordance with the activity than if it were only concerned with satisfying self-paying customers in the open market. As with some businesses, it has different obligations for monies received, dependent on the delivery of special, agreed-upon services as contrasted with monies received from the "sale and delivery" of its regular services.

As further explained later in this chapter in the section "Guide to Fund Accounting," activities of the educational "conglomerate" are generally accounted for in current, loan, endowment, and plant "subsidiaries." The funds received for special, agreed-upon services to be delivered are accounted for as a "restricted" portion of current operations, but could be considered as "deferred revenues" in commercial parlance.

In theory, although fund accounting requires the segregation of resources only as necessary to comply with legal or donor stipulations, in practice most colleges and universities include management and board-designated funds with donor-restricted funds in the separately-accounted-for activities groups. This mixture of externally restricted funds with internally designated funds in the "subsidiaries" necessitates knowledgeable governing board scrutiny to appreciate the quality as well as the quantity of resources available, and the flexibility with which they can be utilized.

Working Capital

Exhibit A, on pages 46-47, begins with the separate balance sheet of Current Funds, the results of operating inflows and outflows, or the "working capital" position of the institution. Assets and liabilities are the same as for a business if the account "Due to other funds" is read as "Due to other subsidiaries" and "Fund balances" are understood as the "working capital" portion of the institution's total net worth, or "equity."

The "restricted" current accounts differ from the unrestricted only to the extent that utilization of the resources has been limited by the provider to a specific activity or area of activity. While such activity is assumed to be a continuing part of the institution's current operations, the institution's need or the donor's requirement for spending the specific restricted funds may extend over one or more operating periods. Until used, such funds provide an important source of working capital.

The current fund balances, both unrestricted and restricted, are key figures in the financial viability of the institution. In addition to acting as working capital, the current unrestricted fund balance, $643,000 in the illustration, represents an accumulated reserve from operations, or "retained receipts" comparable to retained earnings in a business. This most flexible reserve provides both a cushion against future operating deficits and a source of seed money for desirable new programs of instruction, research, and public service.

The current restricted fund balance, $446,000 in the illustration, can be thought of as representing a "backlog" of future business already committed. The extent of management control over the timing and use of these restricted funds determines their flexibility and importance in long-range planning. Just as the adequacy and trends in amounts of working capital and operating reserves in a business must be continually evaluated in terms of sales volume, market risks, inflation, and possible future product needs, so must current fund balances be measured in an educational institution.

The quantity and quality of current fund assets must likewise be routinely reviewed and the offsetting liabilities subjected to board policies and oversight. Excess cash should be temporarily invested in accordance with sound cash management policies and procedures. Receivables must be compared with operating volumes and with those of peer institutions. With more competition for students, colleges and universities—particularly the more expensive independent institutions—are under increasing pressure to provide more student assistance. Receivables are growing and sound collection policies become an increasing responsibility of management. The governing board should receive regular reports on delinquency rates and trends in current student accounts and other significant accounts receivable.

Inventories ordinarily do not represent very large commitments in service institutions; however, any investment in inventories is not available for other purposes and therefore must be justified by relevant

Suggested Questions

economic considerations. The timing of payments should be in accordance with sound disbursement policies and procedures to avoid either uneconomic prepayments or reputation-damaging late payments. All current fund borrowings should be approved by the board. Techniques for managing and protecting current operating assets and working capital funds include appropriate cash flow forecasts, aging reports on receivables, and reviews of significant changes in inventory levels.

So-called "designated" or "allocated" current fund balances should not be allowed to obscure the true unrestricted or restricted nature of current resources. Management, including the governing board, may designate or commit certain resources to specific purposes, but such segregations must be clearly distinguished from external legal or donor restrictions. What management has designated, it can also redesignate, so that until the fund balance has been actually utilized, it remains, in effect, unrestricted. Funds may be designated for special academic or administrative department purposes, or for auxiliary operations or a hospital, to facilitate management control and internal accountability. The board should approve the designation or redesignation of funds and the policy and procedure by which management recommends.

The governing board may "transfer" what might be considered excessive operating reserves, or accumulated current fund balances, to the long-term capital fund groups, with due consideration for any external restrictions applicable. Such transfers of operating reserves would convert them to invested reserves, possibly increasing investment income, but at the expense of operating flexibility. Likewise, the board may "retransfer" any fund balances previously transferred to the long-term capital fund groups back to the current fund balances for needed current expenditures or to make up deficiencies, again with due consideration for any external restrictions applicable. Any retransfer would convert invested reserves to operating reserves, possibly decreasing investment income but increasing operating resources.

The board should not only be aware of but should be required to approve transfers of funds among major fund groups. Examples of such transfers are shown on page 49 in Exhibit B, "Statement of Changes in Fund Balances." While the "Mandatory" transfers are required by debt instruments or third-party providers, the "Unrestricted gifts allocated" of $650,000 represents management transfers of operating funds to loan, endowment, and plant funds, and the "Portion of unrestricted quasi-endowment funds investment gains appropriated" of $40,000 represents a management decision to transfer or retransfer invested funds back to operating funds. Both these transfers should be done with the knowledge and approval of the board in fulfillment of current budgeting and long-range financial plans.

When and to what extent current funds are invested for the future, or invested funds are liquidated to support current operations, are critical decisions for governing boards.

1. Are current fund balances adequate for working capital needs? Has the institution resorted to borrowing for the current fund? From other fund groups or from external sources? Is such borrowing increasing or decreasing?

2. What is the institution's credit rating and reputation among its vendors and in its community?

3. Does the institution have adequate cash management? What is its short-term investment performance? (See Report No. 14 in Chapter 6.)

4. Are receivables and inventories under adequate review and control?

5. Are gift pledges properly recorded, collected, and accounted for?

Exhibit A
Balance Sheet

June 30, 19
with comparative figures at June 30, 19
Sample Educational Institution

Assets	Current Year	Prior Year
Current Funds		
Unrestricted		
Cash	$ 210,000	$ 110,000
Investments	450,000	360,000
Accounts receivable, less allowance of $18,000 both years	228,000	175,000
Inventories, at lower of cost (first-in, first-out basis) or market	90,000	80,000
Prepaid expenses and deferred charges	28,000	20,000
Total unrestricted	1,006,000	745,000
Restricted		
Cash	145,000	101,000
Investments	175,000	165,000
Accounts receivable, less allowance of $8,000 both years	68,000	160,000
Unbilled charges	72,000	—
Total restricted	460,000	426,000
Total current funds	1,466,000	1,171,000
Loan Funds		
Cash	30,000	20,000
Investments	100,000	100,000
Loans to students, faculty, and staff, less allowance of $10,000 current year and $9,000 prior year	550,000	382,000
Due from unrestricted funds	3,000	—
Total loan funds	683,000	502,000
Endowment and Similar Funds		
Cash	100,000	101,000
Investments	13,900,000	11,800,000
Total endowment and similar funds	14,000,000	11,901,000

Liabilities and Fund Balances	Current Year	Prior Year
Current Funds		
Unrestricted		
Accounts payable	$ 125,000	$ 100,000
Accrued liabilities	20,000	15,000
Students' deposits	30,000	35,000
Due to other funds	158,000	120,000
Deferred credits	30,000	20,000
Fund balance	643,000	455,000
Total unrestricted	1,006,000	745,000
Restricted		
Accounts payable	14,000	5,000
Fund balance	446,000	421,000
Total restricted	460,000	426,000
Total current funds	1,466,000	1,171,000
Loan Funds		
Fund balances		
U.S. government grants refundable	50,000	33,000
University funds		
Restricted	483,000	369,000
Unrestricted	150,000	100,000
Total loan funds	683,000	502,000
Endowment and Similar Funds		
Fund balances		
Endowment	7,800,000	6,740,000
Term endowment	3,840,000	3,420,000
Quasi-endowment—unrestricted	1,000,000	800,000
Quasi-endowment—restricted	1,360,000	941,000
Total endowment and similar funds	14,000,000	11,901,000

Annuity and Life Income Funds

	Current Year	Prior Year
Annuity funds		
Cash	$ 55,000	$ 45,000
Investments	3,260,000	3,010,000
Total annuity funds	3,315,000	3,055,000
Life income funds		
Cash	15,000	15,000
Investments	2,045,000	1,740,000
Total life income funds	2,060,000	1,755,000
Total annuity and life income funds	5,375,000	4,810,000

Annuity and Life Income Funds

	Current Year	Prior Year
Annuity funds		
Annuities payable	$ 2,150,000	$ 2,300,000
Fund balances	1,165,000	755,000
Total annuity funds	3,315,000	3,055,000
Life income funds		
Income payable	5,000	5,000
Fund balances	2,055,000	1,750,000
Total life income funds	2,060,000	1,755,000
Total annuity and life income funds	5,375,000	4,810,000

Plant Funds

Unexpended		
Cash	275,000	410,000
Investments	1,285,000	1,590,000
Due from unrestricted current funds	150,000	120,000
Total unexpended	1,710,000	2,120,000
Renewals and replacements		
Cash	5,000	4,000
Investments	150,000	286,000
Deposits with trustees	100,000	90,000
Due from unrestricted current funds	5,000	—
Total renewals and replacements	260,000	380,000
Retirement of indebtedness		
Cash	50,000	40,000
Deposits with trustees	250,000	253,000
Total retirement of indebtedness	300,000	293,000
Investment in plant		
Land	500,000	500,000
Land improvements	1,000,000	1,110,000
Buildings	25,000,000	24,060,000
Equipment	15,000,000	14,200,000
Library books	100,000	80,000
Total investment in plant	41,600,000	39,950,000
Total plant funds	43,870,000	42,743,000

Plant Funds

Unexpended		
Accounts payable	10,000	—
Notes payable	100,000	—
Bonds payable	400,000	—
Fund balances		
Restricted	1,000,000	1,860,000
Unrestricted	200,000	260,000
Total unexpended	1,710,000	2,120,000
Renewals and replacements		
Fund balances		
Restricted	25,000	180,000
Unrestricted	235,000	0,000
Total renewals and replacements	260,000	380,000
Retirement of indebtedness		
Fund balances		
Restricted	185,000	125,000
Unrestricted	115,000	168,000
Total retirement of indebtedness	300,000	293,000
Investment in plant		
Notes payable	790,000	810,000
Bonds payable	2,200,000	2,400,000
Mortgages payable	400,000	200,000
Net investment in plant	38,210,000	36,540,000
Total investment in plant	41,600,000	39,950,000
Total plant funds	43,870,000	42,743,000

Agency Funds

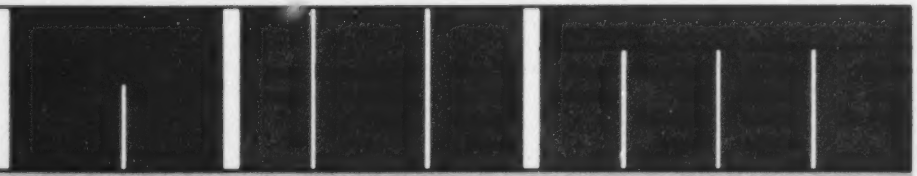
Cash	50,000	70,000
Investments	60,000	20,000
Total agency funds	110,000	90,000

Agency Funds

Deposits held in custody for others	110,000	90,000
Total agency funds	110,000	90,000

See accompanying Summary of Significant Accounting Policies and Notes to Financial Statements on pages 95-97.

Exhibit B
Statement of Changes in Fund Balances
Year Ended June 30, 19__
Sample Educational Institution



Revenues and Other Additions									
Unrestricted current fund revenues	$7,540,000								
Expired term endowment—restricted						$ 50,000			
State appropriations—restricted						50,000			
Federal grants and contracts—restricted		$ 500,000							
Private gifts, grants, and contracts—restricted		370,000	$100,000	$1,500,000	$800,000	115,000		$65,000	$ 15,000
Investment income—restricted		224,000	12,000	10,000		5,000	$ 5,000	5,000	
Realized gains on investments—unrestricted				109,000					
Realized gains on investments—restricted			4,000	50,000		10,000	5,000	5,000	
Interest on loans receivable			7,000						
U.S. government advances			18,000						
Expended for plant facilities (including $100,000 charged to current funds expenditures)									1,550,000
Retirement of indebtedness									220,000
Accrued interest on sale of bonds								3,000	
Matured annuity and life income restricted to endowment				10,000					
Total revenues and other additions	7,540,000	1,094,000	141,000	1,679,000	800,000	230,000	10,000	78,000	1,785,000
Expenditures and Other Deductions									
Educational and general expenditures	4,400,000	1,014,000							
Auxiliary enterprises expenditures	1,830,000								
Indirect costs recovered		35,000							
Refunded to grantors		20,000	10,000						
Loan cancellations and write-offs			1,000						
Administrative and collection costs			1,000					1,000	
Adjustment of actuarial liability for annuities payable					75,000				
Expended for plant facilities (including noncapitalized expenditures of $50,000)						1,200,000	300,000		
Retirement of indebtedness								220,000	
Interest on indebtedness								190,000	
Disposal of plant facilities									115,000
Expired term endowments ($40,000 unrestricted, $50,000 restricted to plant)				90,000					
Matured annuity and life income funds restricted to endowment				10,000					
Total expenditures and other deductions	6,230,000	1,069,000	12,000	90,000	85,000	1,200,000	300,000	411,000	115,000

Transfers Among Funds—Additions/(Deductions)									
Mandatory:									
Principal and interest	(340,000)							340,000	
Renewals and replacements	(170,000)						170,000		
Loan fund matching grant	(2,000)		2,000						
Unrestricted gifts allocated	(650,000)		50,000	550,000		50,000			
Portion of unrestricted quasi-endowment funds investment gains appropriated	40,000			(40,000)					
Total transfers	(1,122,000)		52,000	510,000		50,000	170,000	340,000	
Net increase/(decrease) for the year	188,000	25,000	181,000	2,099,000	715,000	(920,000)	(120,000)	7,000	1,670,000
Fund balance at beginning of year	455,000	421,000	502,000	11,901,000	2,505,000	2,120,000	380,000	293,000	36,540,000
Fund balance at end of year	643,000	446,000	683,000	14,000,000	3,220,000	1,200,000	260,000	300,000	38,210,000

See accompanying Summary of Significant Accounting Policies and Notes to Financial Statements on pages 95-97.

Flow of Funds
From Source to Resource

Long-Term Capital

Long-term capital is required to finance assets that will not be recovered or converted to cash within the normal operating cycle. These assets include land, buildings, and equipment; student loans; and investments that provide an earnings base independent of current supporters. Long-term capital is provided directly by gifts and government appropriations, or indirectly through current operating funds.

Current operating funds may be expended for equipment and minor plant renovations directly from current accounts; or they may be transferred to the plant funds group, to be expended from there for debt service, major plant additions, and renewals and replacements, or to loan funds, or to endowment and similar funds, either as required by external agreements or benefactors (mandatory transfers), or as determined by management.

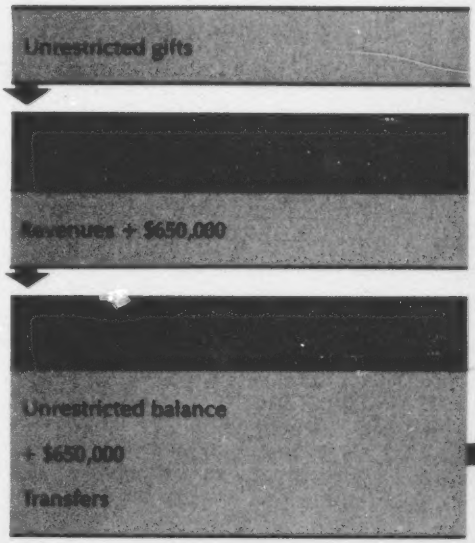
The Statement of Changes in Fund Balances referred to above shows these flows of long-term capital. Under "Revenues and other additions," supporters with "Private gifts, grants, and contracts—restricted" directly provided $100,000 to loan funds, $1,500,000 to endowment and similar funds, $800,000 to annuity and life income funds, $115,000 to funds for spending on plant, $65,000 for retirement of indebtedness, and $15,000 of "in kind" plant or equipment. An "Expired term endowment" provided $50,000 directly for plant. "State appropriations" provided another $50,000 for plant expenditures. "Investment income—restricted," "Realized gains on investments," and "Accrued interest" provided a total of $16,000 in "capital" to loan funds, $169,000 to endowment and similar funds, and $38,000 to the various plant funds.

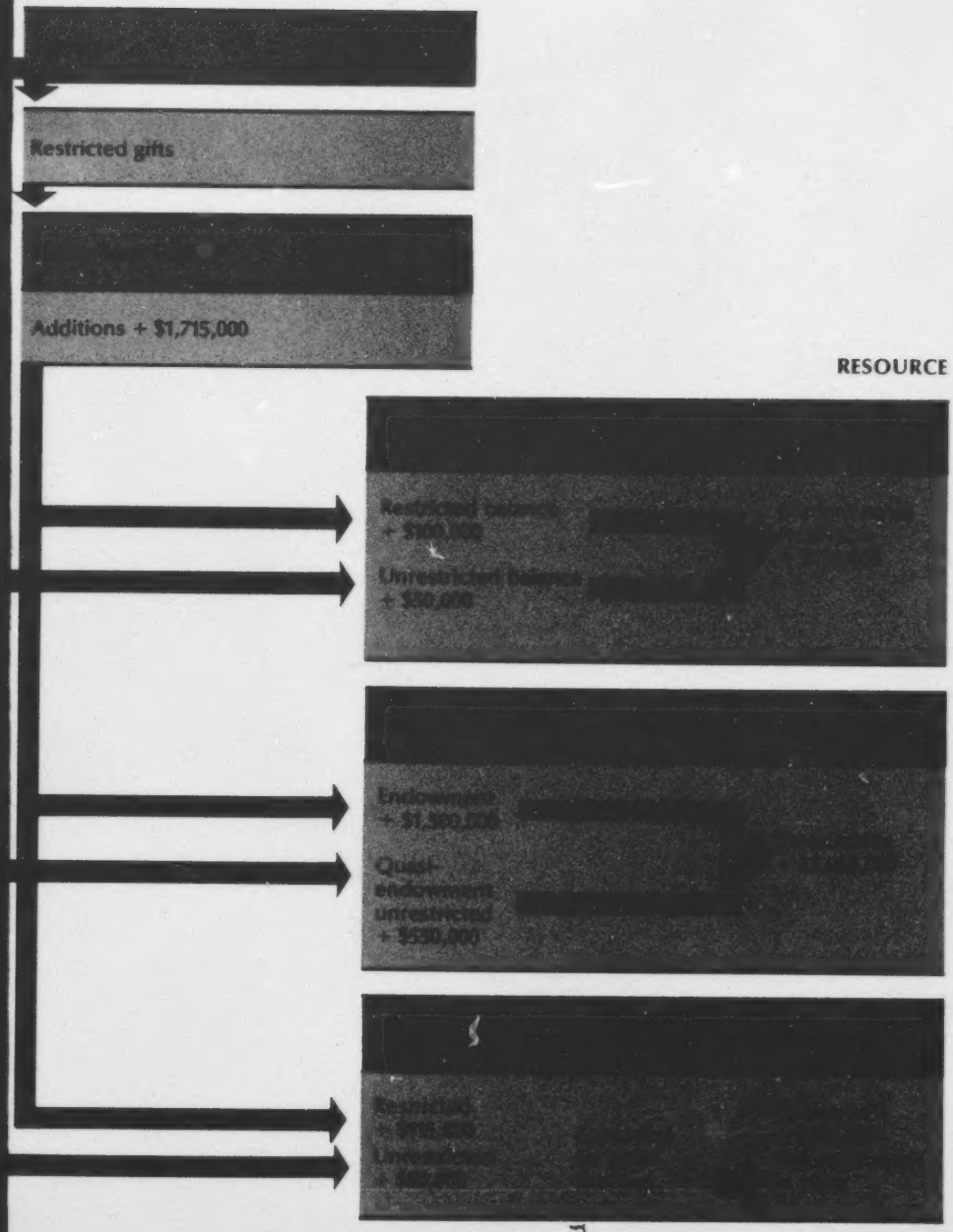
Below the "Expenditures and other deductions" section, the "Transfers among funds" include the long-term capital provided through current operations. Mandatory amounts of $340,000 for debt service ("Principal and interest") and $170,000 for "Renewals and replacements" were transferred as required to plant funds, while $2,000 was transferred to loan funds for a matching grant. In addition, nonmandatory transfers of "Unrestricted gifts," which might be considered current operating "surpluses," were made by management in the amount of $650,000, of which $50,000 was designated for loan funds, $550,000 for quasi-endowment, and $50,000 for plant. Offsetting this was $40,000 as "Portion of unrestricted quasi-endowment funds investment gains appropriated," or transferred from long-term invested funds to current use.

The inflows of long-term capital directly and indirectly into the capital fund groups, less the outflows indicated, are important considerations for the administration and governing board in the long-range planning and budgeting for any educational institution. A minimum understanding of the Statement of Changes in Fund Balances is necessary in tracing capital from source to resource (see the accompanying figure on flow of funds).

The concept of operating surpluses funding fixed assets is familiar to business-oriented trustees but the reporting of such in terms of fund accounting in a nonprofit organization is generally not well understood by governing boards. Board members have a right, indeed a duty, to require management to report and to explain adequately past, present, and anticipated funds flows.

The results of the changes in fund balances are shown in Exhibit A, "Balance Sheet." The assets, liabilities, and fund balances, or "equity" of the long-term capital fund groups, are shown in a series of segregated balance sheets, one for each group, layered pancake-fashion under the Current Funds balance sheet.





Loan Funds

The Loan Funds balance sheet reports the assets, liabilities, and fund balances of the institution's "lending subsidiary," maintained principally to help its students finance their education. This capital in recent years has been provided increasingly by the federal government and accounted for variously as refundable advances (liabilities) or restricted grants (fund balances). Loan funds specifically provided by interested private benefactors become restricted fund balances. The institution often must add "matching" funds, which then become restricted, or it may transfer unrestricted current funds to increase "unrestricted" loan resources. These inflows and some examples of outflows of loan funds, by refunds or write-offs, are illustrated in the Statement of Changes in Fund Balances.

As the government has provided more and more of the loan resources, it has increased its demands for more businesslike policies and procedures in both lending and collecting. The inherent problem is that lending to students is supposed to be based more on need than on any indicated ability to repay, a much different premise than in commercial lending. Separate audits of the government's loan funds are required, and inadequate accountability can result in loss of government support.

Because loan funds are revolving, and availability to future students depends on repayments from former students, and because there are never enough funds, it behooves management and the governing board to monitor closely the lending procedures, aging of student notes receivable, delinquency rates, collection procedures, refunds, and write-offs, regardless of whether government or institutional funds are involved. Loan funds could be considered student resources as well as institutional resources, but they serve all by encouraging the enrollment of worthy students of limited financial means. Loan

resources should be continually sought and carefully preserved to maximize student benefits.

Endowment and Similar Funds

The next long-term capital, "subsidiary" balance sheet in Exhibit A includes endowment and similar funds. Nowhere else is the governing board's constant dilemma of having to choose between obligations to present versus future constituencies brought more sharply into focus than in its management of endowment and other long-term invested funds.

While true endowment has been limited by the donors to providing the capital base of the institution, quasi-endowment (or funds functioning as endowment) has been "retained" from prior years' operations by management decision to support future operations. Most independent colleges and universities would not exist were it not for the thrift and foresight of earlier administrators and governing boards. Endowment and similar funds are the resource that enables an institution to be independent; the more endowment, the greater the independence. Higher education is founded on independence—in thought, word, and deed.

Endowment enables an institution to provide more services to more of its constituencies at less than self-supporting prices. It can mean the difference between survival and bankruptcy when financial viability is threatened. It is the fundamental "net worth" of the independent college or university, which cannot depend on public funds to subsidize its educational efforts.

Its management should be one of the more natural responsibilities for the typical business-oriented trustee, but it is also one of the most controversial. Does the institution save some of its current resource inflows for the future? How much? If not, how would there ever have developed a Harvard? A Yale? Does the institution invest its savings, i.e., its "surpluses," to maximize present income to support current operations, or to provide for growth in capital to support future operations? If both, in what proportions? Does the institution compromise on a "total return" approach? How does it cope with inflation, money rates, and securities market fluctuations over which it has no control?

Who should be responsible for the management and protection of endowment and similar funds? The board itself? A committee of the board? Internal or external professional investment managers? What are the agreed-upon objectives, guidelines, policies, and procedures? How should such investment management be monitored and evaluated?

Before members of the governing board can fulfill their responsibilities for long-term capital, they must be able to read the balance sheets and other financial statements of educational institutions to know what capital is available, where it comes from, and under what circumstances it can be used. Earlier in this chapter it was shown how current funds could flow into long-term capital fund groups for investing in student loans, securities, or plant facilities. Such investments can be liquidated later and returned to working capital, but perhaps at very different values than when earlier committed to the long term. Long-term capital, like working capital, is variously obligated to different causes in colleges and universities. The governing board must be aware of the practical limitations on use under these obligations.

Annuity and life income funds, which are trust funds, are a special group of invested funds temporarily committed to supporting donor-designated beneficiaries. "Temporarily" means for the lifetime of the beneficiaries, or until specific time periods have expired, after which the remaining funds become institutional capital, operating or long-term, unrestricted or restricted, depending on the agreements with the donors. Annuity and life income agreements, investment management, and reporting obligations to both donors and beneficiaries involve substantial legal, accounting, and tax considerations. The governing board should be sure that adequate professional expertise has been made available and followed in soliciting, accepting, and managing annuity and life income funds, for the board is responsible to more than the institution. The institution's "equity" is a future one, the timing and amounts of which are uncertain, but dependent on good management.

Of the $2,505,000 shown as annuity and life income fund balances at the beginning of the year in the Statement of Changes in Fund Balances, only $10,000 "matured" and, as restricted, moved to endowment for institutional use. A total of $800,000 was received under new agreements, and an additional obligation of $75,000 in "actuarial liability" was recorded, resulting in ending fund balances of $3,220,000.

Plant Funds

Colleges and universities, as distinct from profit-oriented enterprises, (or even some nonprofit-oriented ones, such as hospitals), have traditionally segregated their plant funds accounting and have generally ignored depreciation. The reason is that most plant funds were originally given or appropriated as restricted or, if not, have been so irrevocably committed to fixed assets that they will never be available for any other purpose. If the resulting plant has been donated, the institution cannot very easily justify charging for depreciation, or expecting "customers" to pay for something that was given in the first place to help those customers.

On the other hand, as shown earlier, some colleges and universities not only make capital expenditures out of current operating accounts, but transfer operating funds to plant for debt repayments and plant renewals and replacements, which could be considered

tantamount to a flow of depreciation-like expenses. The flows of funds into and out of plant accounts, and the resulting plant assets and fund balances, or equity, are important in the management and protection of that part of the institution's long-term capital.

How much have external sources contributed directly to plant funds compared with amounts of current operating funds transferred to plant during the fiscal year? Referring to the top section of the Statement of Changes in Fund Balances, $230,000 in new funds was added directly to unexpended plant funds from various sources as indicated. Under the transfers section at the bottom, $50,000 in unrestricted gifts was allocated by management decision from current to plant funds. Out of these receipts and the prior unexpended balance of $2,120,000, a total of $1,200,000 was "Expended for plant facilities" (under "Expenditures and other deductions" in the middle section of the statement), leaving an "Unexpended" balance at the end of the year of $1,200,000, available for future plant needs.

Similarly, $10,000 in new funds was received directly for "Renewals and replacements" and $170,000 was transferred from current funds under third-party requirements (mandatory). Out of these receipts and the beginning fund balance of $380,000, a total of $300,000 was "Expended for plant facilities," leaving an ending balance of $260,000 for future renewals and replacements. "Retirement of indebtedness" received $78,000 in new funds from external sources and $340,000 in mandatory transfers from current operations for "Principal and interest." Out of those inflows and the $293,000 beginning balance, the institution's debt service obligations on its plant were fulfilled (under "Expenditures and other deductions" in the middle of the statement), and $300,000 in debt service funds remained for the future.

The last column shows the changes in the institution's net investment, or equity, in its physical facilities, that is, in its accumulated historical plant cost less associated liabilities. Of the year's additions to net "Investment in plant," $15,000 was from gifts in kind, $1,550,000 from expenditures by the other plant fund groups and from current funds, and $220,000 from retirement of indebtedness. During the period, $115,000 of plant facilities were disposed of, for a net addition of $1,670,000 and an ending balance of $38,210,000 (see the accompanying figure of flow of plant funds).

The governing board and the administration must be aware of the total and mix of plant funds. Beginning plant fund balances totaled $39,333,000. For all the above additions and deductions, the ending plant fund balances, or equity in all plant funds, increased only $637,000, to a new total of $39,970,000. It should be noted that only $1,460,000 of the most flexible "unexpended" and "renewal and replacement" funds remained, compared with $2,500,000 at the beginning of the period. The difference has been irrevocably committed to "bricks and mortar" or equipment.

Many donors, faculty members, students, and even trustees do not realize that depreciation, or the cost of wear and tear on physical facilities, is not usually accounted for in tuition and fee charges or in the expenditures of colleges and universities.

In the Statement of Changes in Fund Balances, the total of current operating funds made available for plant capital included: expenditures from current accounts, $100,000; mandatory transfers for debt retirement (not interest), $220,000, and for renewals and replacements, $170,000; and "allocated" to plant, $50,000. If these were added, how would the total of $540,000 compare with a reasonable wear-and-tear cost, or replacement cost, as a percentage of the total investment in plant? During this particular period, and for similar amounts over time? Such amounts funded from current operations, but really expended for plant, could be considered capital expenditures "in lieu of depreciation." In the year illustrated, it would represent only 1.35% of the total investment in buildings and equipment, based on the balance sheet amount in Exhibit A.

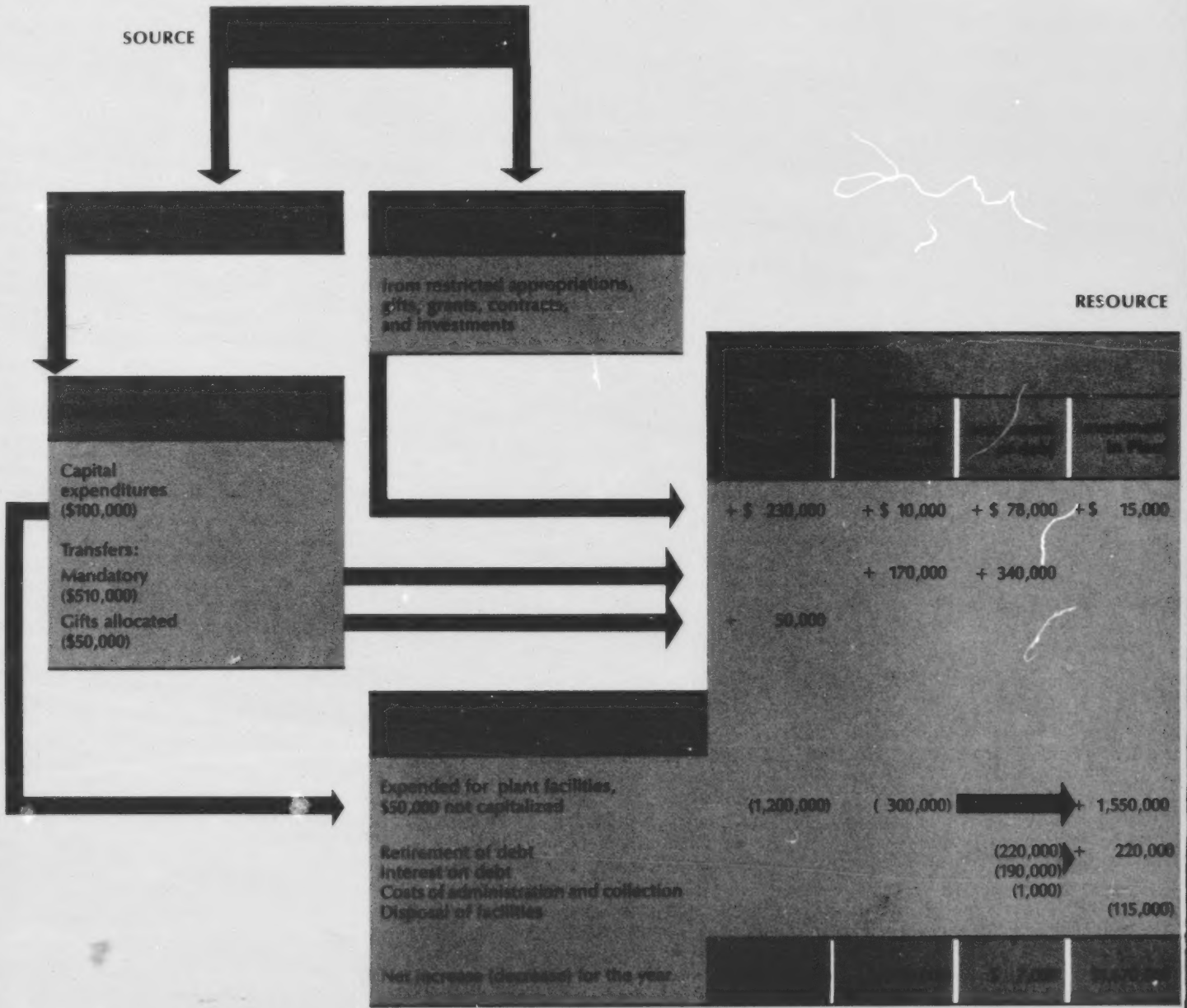
The illustrative institution obviously depends heavily on funds from external sources for plant maintenance as well as plant additions. Unfortunately, externally restricted funds are more likely to be given for additions than for preservation of current physical facilities. Over time, this can result in gradual deterioration of buildings and equipment not recognized in either operating statements or balance sheet valuations.

The governing board must be aware of the danger of increasing amounts of deferred maintenance through inadequate budgeting for plant renewals and replacements from current operating accounts. As plant facilities that were added in the 1950s and 1960s wear out, capital fund drives specifically for rehabilitation and replacement may be necessary. Additional buildings may have to be limited to those for which maintenance funds are also made available.

Management must plan and budget capital expenditures as realistically as operating expenditures, with the anticipated revenues or plant additions to cover, and must explain the needs to the institution's constituency. Needs should be related to programs through allocations of space and equipment to departments. Utilization of present space and equipment should be justified as critically as requests for new items.

Flow of Plant Funds

From Source to Resource



Total Capital

Some appreciation of the adequacy of the financial resources of an institution might be revealed in trends of the fund balances, the institution's capital or net worth, in mix and in total, over the years (see Report No. 18 in Chapter 6). More "prior year" figures could be added to those extracted from Exhibit A, "Balance Sheet," as follows:

	Current year	Prior year
Current fund balances—unrestricted	$ 643,000	$ 455,000
Current fund balances—restricted	446,000	421,000
Total "working capital"	1,089,000	876,000
Loan fund balances	683,000	502,000
Endowment and similar fund balances	14,000,000	11,901,000
Annuity and life income fund balances	3,220,000	2,505,000
Plant fund balances:		
Excluding net investment in plant	1,760,000	2,793,000
Net investment in plant	38,210,000	36,540,000
Total capital, equity, or "net worth"	$58,962,000	$55,117,000

As in profit-oriented businesses, "working capital" can be compared with operating budgets, currently and over the years. The endowment and similar fund balance can be compared with numbers of students, tenured faculty, indebtedness, and other kinds of long-term obligations. It might be discounted for losses in purchasing power of the dollar. It should be measured for its relative contribution to current operating budgets over the years. Uncommitted plant funds can be compared with net investment in plant and with debt service requirements to estimate adequacy in covering anticipated capital outflows for plant replacements and debt retirement.

Again, as in any business, debt amounts and trends can be measured for reasonableness against the assets financed by debt. Debt service costs can be measured against additional revenues or net cash flows anticipated from the assets financed. Debt can also be compared with totals of unrestricted and restricted funds that could be made available for repayment. It should be noted that although there may be unrestricted fund balances in the various fund groups, such amounts may not be in cash or be readily convertible into cash for other purposes. As in any business, the assets of a college or university have varying degrees of liquidity with quite different "book," "going concern," and "liquidation" values.

Long-term Debt

Incurring indebtedness may be a cost-effective solution to obtaining necessary facilities expansion or replacement. However, assumption and payment of principal and interest require careful consideration of need, sources of funds, and possible limitations of funding agencies. The governing board and administration should agree on policies and procedures for incurring debt. Any collateral offered must be reviewed for third-party restrictions. Limitations on types or levels of debt should be established by the board. Operating and maintenance costs of the additional or replacement facilities must be considered as well as the debt service requirements.

1. Has the growth in student loan capital kept pace with the increase in numbers of students and average tuition and fees charged? Has the administration done all it can to seek new loan funds and to preserve present ones? What have been the reports of government-required audits of loan funds?

2. How much in current funds has been transferred to quasi-endowment for investment to support future operations? How has the growth in endowment capital kept pace with inflation? How has income from endowment maintained its proportional contribution to current operating budgets?

3. Have solicitation materials, accounting, and reporting for annuity and life income funds been approved by knowledgeable persons, including the governing board?

4. Has management adequately explained the flow of funds to preserve plant capital? How does the amount funded from current operations compare with "depreciation"? What is the justification process for investment in new facilities? Does the governing board have to approve all major gifts in kind? Plant additions? Renovations? Disposals? Is there agreement as to what is "major"?

5. Does the governing board approve all borrowing agreements? Is debt increasing or decreasing as a percentage of investment in plant? Is debt service increasing or decreasing as a percentage of current operating budget?

6. What have been the trends in working and long-term capital over the years? (The mix of working and long-term capital may determine the degree of financial viability of the institution.)

Protecting Resources

Protecting the institution's resources and avoiding potential liabilities is an important responsibility of the governing board. The administration recommends internal control policies and practices for financial, administrative, and operational activities, and the board is responsible for approving them. There are many policies to consider, but the only ones discussed in this section relate to audits, risk management and insurance, patents and copyrights, and legal counsel.

Audits

The governing board should be assured that the institution's activities are subject to audit. Audits may be performed in separate but coordinated efforts by internal and external auditors (the latter includes public accounting firms and state and federal auditors).

Audits performed by both internal and external auditors are designed to ascertain that the overall system of internal control is adequate, effective, and functioning to safeguard the institution's resources. They should also determine that financial transactions are properly approved, recorded, summarized in the records, and properly classified in reports. The auditors should see that financial transactions are in accordance with the policies of the board and that they comply with applicable laws, regulations, and donor restrictions.

Internal and external auditors are not in competition with each other; rather, the internal audit team complements the external auditors. While a close relationship should exist, there are distinct differences because their work varies in scope and final objectives: internal auditors perform detail reviews of activities of the institution to apprise management of the adequacy of controls, policy compliance, procedures for safeguarding assets from fraud, and sometimes performance of employees in carrying out assigned responsibilities; independent external auditors attest that the financial statements of the institution are prepared in accordance with generally accepted accounting principles applied on a consistent basis.

The external audit should include tests and evaluations of internal controls and of compliance with financial policies; such an audit should also include a management letter. Most of the tests are similar to but less extensive than those performed by the internal audit group. Work of federal and state auditors, which is also identified as external, typically concerns specific activities, and thus more clearly relates in objective and scope to that of internal auditors.

The governing board, through the establishment of an audit committee or by other means, should stress the importance of the audit function and should meet with the internal and external auditors to discuss material findings and recommendations. This committee should fully understand the audit procedures required to render an opinion. Discussions are encouraged both before the audit begins and after it is completed to provide the necessary level of assurances desired by the committee. The committee should meet with management to determine the actions taken on comments included in the management letter of the external auditors.

The audit committee recommends and the governing board should appoint the external audit firm. The firm should be chosen based on the quality of its staff, its audit program, and on economic considerations. The board or audit committee should review the scope of both internal and external audit plans prior to implementation and should request any special audits to be undertaken.

Persons performing the internal audit may report to either the chief business officer or the president of the institution, depending on the supervisory capacity of the manager of internal audit and/or the president's interest in overseeing the internal audit function. In either case, the governing board should require that the internal audit function have formal access directly to the audit committee and to the president.

The governing board may find that supplementary schedules would be helpful for relating audited reports to the budget. If so, such schedules should be requested of the auditors or the chief business officer.

Risk Management and Insurance

The governing board should be apprised of the risks and potential losses the institution may encounter. Generally, these risks are not predictable and include (1) claims that charge mismanagement, malpractice, discrimination, or copyright infringement, (2) uninsured losses against theft or catastrophe, and (3) deductibles on insurance claims. Risk management includes a systematic and continuous identification of potential risks and adoption of the following:

- Financial, administrative, and academic policies.
- Good security.
- Personnel policies.
- Safety program.
- Inspection program.
- Adequate insurance coverage.

Some risks having minimal loss potential or predictable costs may be absorbed through the operating budget. Other risks, which are too infrequent to be predictable and too large to be financed internally, require funding by self-insurance reserves or by obtaining insurance coverage.

The board should be aware, through periodic reports of the various levels and kinds of risks, of management's plans for handling the risks and of how the plans are to be financed. The effect of inflation on the value of property and the size of potential claims should be closely monitored.

Suggested Questions

1. Does the audit committee annually review the scope of the external and internal audit programs?

2. Does the audit committee review management's responses to the written comments of the internal and external auditors with respect to internal control weaknesses, operating efficiencies, and the condition of the institution's resources?

3. What risks are self-insured by the institution? Are adequate reserves maintained?

4. What are the results of reviews undertaken to determine potential risks such as malpractice, discrimination, fire, and theft? What actions have been taken to reduce exposures?

5. What is the institution's policy for the identification and ownership of patentable inventions?

6. Does the institution conduct audits of patent licenses in accordance with its rights included in the license agreements?

7. Has the institution's legal counsel reported to the board on the status of pending legal matters?

Patents and Copyrights

The governing board should be assured that all inventions and copyrightable material of value belonging to the institution have been protected through patents and copyrights. This requires the adoption of policies and practices for identifying material subject to patents and copyrights. It also requires professional expertise to adequately process applications and manage any patent or copyright material.

Patent and copyright policies should establish and define the rights and obligations of sponsors, the institution, and its employees. Such policies should expressly state ownership rights, distribution of royalties, and any obligation to market original work.

Legal Counsel

More than ever before, colleges and universities are involved in legal matters. This is due to many factors, among them an increasingly litigious society and more federal and state laws affecting higher education, especially with respect to personnel and students. In protecting the institution's resources, the governing board has an obligation to insure that all legal matters are reviewed by counsel. Contracts entered into by the board are an example; these may commit the board for many years.

Every institution should have a lawyer. Staff counsel, external counsel, or both may be used, the choice depending largely on the size of institution and on the specialties required. State attorneys general sometimes act as counsel for public institutions, and in some independent institutions, legal services are provided by one or more members of the board. Whether counsel is internal or external, one person in the administration should be the coordinator of all legal concerns, acting as liaison to the legal adviser.

Guide to Fund Accounting

The principles of fund accounting for colleges and universities are contained in NACUBO's *College and University Business Administration* (1974) and in several other authoritative references. The following explanation of fund accounting emphasizes how to read financial statements presented in a fund accounting format.

Classification by Restriction

The principles of fund accounting evolved from fiduciary responsibility; their purpose is to insure that financial resources are managed in fulfillment of the obligations attached to them. Fund accounting allows for the orderly separation of resources whose uses are externally restricted from resources that have no restrictions on use. Since funds entrusted to a governing board are often for a specific purpose, such as student financial aid, a new building, or a specific research project, the board and administration require a method to systematically account for funds having such restrictions.

Classification by Fund Group

In addition to being restricted and unrestricted, funds are also classified into *fund groups* that reflect the purpose of the resources. For example, all resources that are to be spent for construction of buildings are shown in a Plant Funds group. These separate fund groups can be displayed in columns having the following labels, although additional columns may be appropriate, depending on the institution:

- **Current Funds**
- **Student Loan Funds**
- **Endowment and Similar Funds**
- **Plant Funds**

Current Funds. These funds have been given or paid to the institution in support of its current operations. They can be used for

such purposes as paying salaries, buying equipment, and providing scholarships and fellowships. It is this column that is managed through the operating budget process; it also contains some of the savings the institution has accumulated that may be used to support future operations.

The current funds column is divided to recognize restrictions and other limitations that donors, payers, or trustees have attached to the funds. This classification can be displayed as follows:

Current Funds		
Unrestricted		Restricted
Not Designated	Designated	

Unrestricted funds can be classified into those that are *designated* and those that are *not designated*. The "Designated" column is for funds the institution rather than an external source has specified are to be used or saved for a particular purpose. The financial activities of self-supporting activities such as hospitals, residence halls, and bookstores could be shown in this column. Also, if a department or other entity has been allowed to accumulate savings from unrestricted sources to use for its own purposes, that amount could be shown here. The "Not Designated" column is for funds that can be used for any institutional purpose; typical sources of such funds are tuition, appropriations, and unrestricted gifts from donors. Report Nos. 15-18 in Chapter 6 illustrate the various classifications discussed above.

Student Loan Funds. The funds in this column cannot be spent for operations, but are lent to students to assist them with their costs of education. These funds come from such sources as private donors and the federal government; another source is the institution itself, where they may have been designated by the governing board for this purpose. As these loans are repaid, the principal and interest are lent to other students.

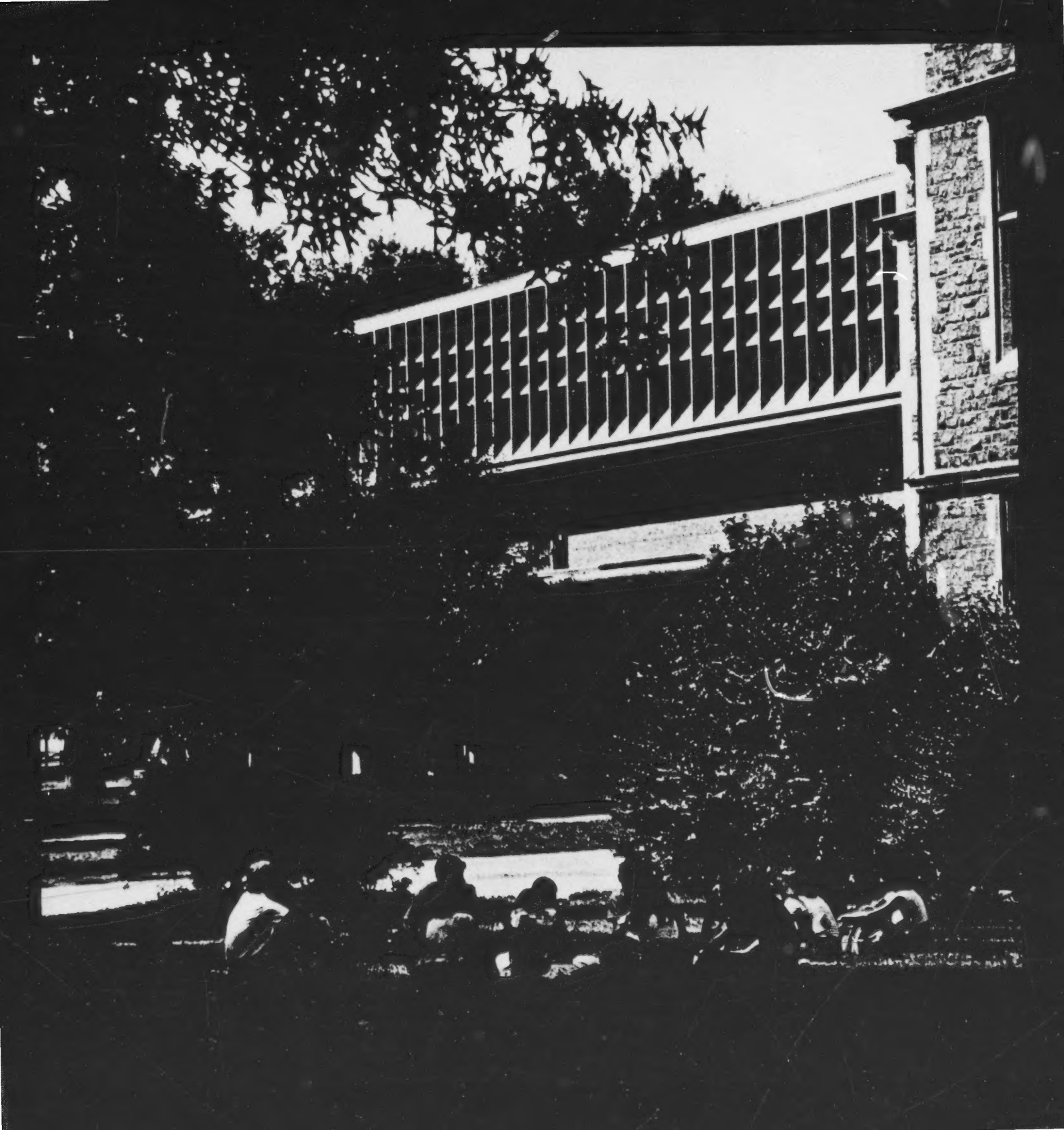
Endowment and Similar Funds. Endowment funds are received from donors on the condition that the gift be maintained in perpetuity (true endowment) or for a specified period of time (term endowment). Also in this column, but separately identified in Reports Nos. 15, 16, and 18 in Chapter 6, are quasi-endowment funds, which the governing board has decided to treat as though they were endowment, and funds that have annuities or life income trusts attached to them. (If material in amount, annuity and life income funds could be a separate fund group, as shown in Exhibits A and B earlier in this chapter.) Endowment income that can be used for current purposes (either restricted or unrestricted) is recorded in the appropriate current funds column.

Plant Funds. The plant funds are divided between unexpended funds and those previously invested in equipment, buildings, and grounds, as follows:

Plant Funds	
Unexpended	Investment in Plant

Unexpended plant funds are those that have been received for buildings or other facilities, along with funds the governing board has designated to be used for improving the facilities or for the repayment of debt. When these funds have been used for construction or debt repayment, the value of the new or paid-for facility is added to the "Investment in Plant" column at its new or paid-for cost. (The authoritative references have separate fund subgroups for renewals and replacements and for retirement of indebtedness, as can be seen in Exhibits A and B earlier in this chapter; for purposes of this discussion, however, they are merged with the unexpended plant funds.)

Note: The section "Results of Operations" on pages 81-86 continues the explanation of how each of the funds mentioned above can be reported to the governing board.



Chapter 5 Planning and Budgeting

The previous chapters have discussed some of the management issues affecting the revenues, expenditures, and financial resources of the institution. These issues should be systematically addressed through the establishment of policies and the implementation of a sound planning and budgeting process. An active and committed governing board, interested in understanding the issues facing the institution, is a valuable asset to the planning and budgeting process.

The governing board has several responsibilities to fulfill in assuring itself that the long-range plans and budgets have been effectively developed. These include:

- Organizing itself to effectively address the planning and budgeting activities. For most boards this would involve establishing a committee that would be responsible for detailed briefings to the full board. For many boards it would involve coordinating the committees having responsibility for various aspects of the plans and budgets, such as the academic program committee, finance committee, and buildings committee.
- Developing, with the administration, a planning and budgeting calendar of when decisions on such items as tuition rate, endowment payout, salary increases, and proposed new programs must be brought to the board for consideration. The calendar will vary among institutions because the sequence of events is affected by such factors as the governmental legislative process, academic calendar, and number of board meetings per year.

The value of planning and budgeting is that it provides the focus for directing the accumulation and use of resources in a way intended to be most beneficial to the institution's mission. When the board can assure itself that planning and budgeting are major undertakings of the administration and that they actually serve as the context for future decisions, then there is good reason to believe the institution has the structure for good management.

In addition to seeing that the institution and the board have been organized to emphasize planning and budgeting, the board has other opportunities for contributing to the planning and budgeting process. One of these is to examine the context in which the plans and budgets are being developed. Two natural issues to examine, as mentioned in Chapter 1, are the institution's mission and its environmental conditions.

Reviewing the institution's mission. At the beginning of each planning cycle, the board should be asked to review and assess the institution's mission (see the first part of Report No. 2, "Statement of Mission," in Chapter 6). The purpose of this review is to reconfirm that the institution's mission continues to be based on a societal need and that the need will continue. The board should verify that the institution's activities have been consonant with the mission and that there are no major weaknesses. (Much of the material contained in Chapter 1 and in Report No. 1, "State-of-the-Institution Report," in Chapter 6, is useful for this appraisal.) The board, as overseer, assumes the ultimate responsibility for either keeping the institution moving in the direction of its mission or going through the complex process of reappraising the adequacy of the mission as it currently exists.

Evaluating the impact of environmental conditions. The environmental factors outlined in Chapter 1 and illustrated in Report Nos. 3 and 4, "Environmental Assumptions," in Chapter 6 are of critical importance to the board; they provide a background for creating the plans and budgets. During the early stages of each planning cycle the board, with the administration, should have the opportunity to decide how such factors as national enrollment trends, inflation, energy, and federal government priorities are expected to affect the institution. Especially for public institutions, the actions (and anticipated actions) of state and local governing authorities need to be well understood and their effect measured. If the board understands these influences, it can knowledgeably examine and ultimately approve the plans and budgets. In many respects, these resulting documents will be reactions to the anticipated effects of the external conditions.

Up to this point in the process, the board has been shown to have a useful role in providing leadership for planning and budgeting, based on an understanding of the context in which plans and budgets are created. In the next stage of the process, the board has the opportunity to directly influence the course of the institution. This substantive role involves at least three issues:

1. Evaluating competing program goals. Governing boards should anticipate that there will always exist a healthy competition among program priorities. The planning process provides the occasion to evaluate existing programs—academic as well as support—to determine their effectiveness and whether they should be continued. Programs should be periodically examined in detail, possibly through the establishment of self-study groups involving faculty, students, administrators, and trustees. The self-study analysis would evaluate the academic strength, content, and resources used for the program and compare it with similar programs in other institutions. The board should actively encourage a systematic analysis of existing programs.

2. Reviewing proposals for new programs. During the planning and budgeting process, the governing board has the responsibility to review proposals for new programs. These proposals may include new departments, research centers, and degree programs that will commit the institution to the expenditure of substantial resources. The board should evaluate the merit of such proposals in relation to the institution's mission. It should also critically examine the long-term financial

obligations inherent in these proposals, which may include additional facilities, tenured faculty, and administrative and support costs. The board should examine the feasibility of any proposed increase in tuition, activity fees, appropriations, and sponsored project revenues designated to pay for the cost of the new programs.

3. Balancing the future against the present. The governing board assumes the difficult task of balancing current and future needs. Such decisions as (1) spending accumulated reserves to balance the budget, (2) increasing tuition, (3) implementing major renovation programs, and (4) determining the amount of unrestricted gifts to save involve judgment as to whether resources should be spent now or protected for future student generations. The decisions made in these areas will greatly depend on the environmental factors described in Chapter 1 and illustrated in Report Nos. 3 and 4 in Chapter 6. Related to this issue is the subject of financial viability; the planning process should be the occasion for evaluating the adequacy of such items as size of the endowment, condition of physical plant, and amount of working capital.

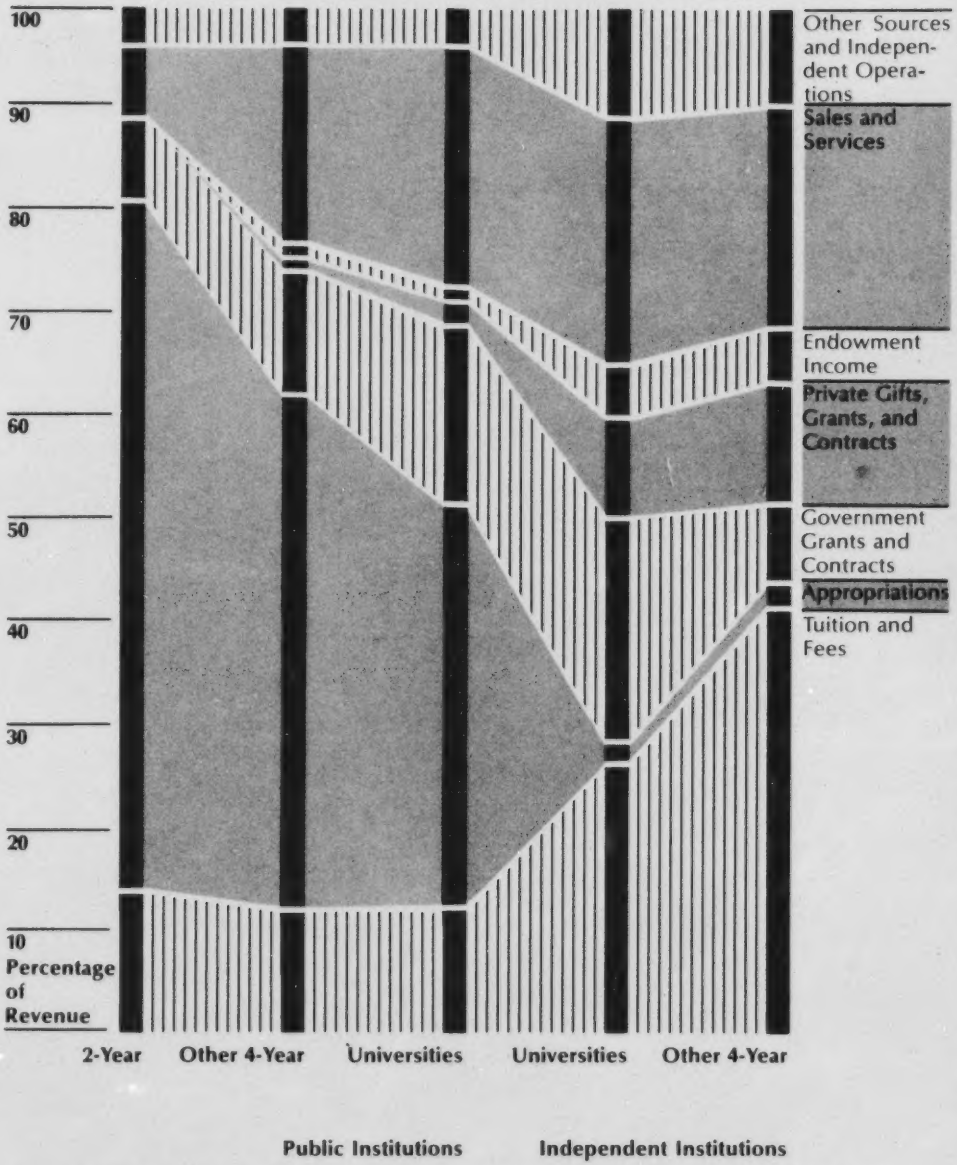
The board's program review, evaluation, and decisions depend on the development of effective and well documented "decision packages" prepared by the administration. The introduction to this monograph described several principles and techniques for improving presentations at this important and difficult stage of the planning and budgeting process.

At the time the governing board is examining the program aspects of the institution's plans and budgets, it also needs to understand the financing strategy. This can be defined as the plan that identifies the revenue sources available and describes how they are combined to finance the programs.

The accompanying figure shows the diverse (but not unexpected) funding patterns

Comparative Sources of Revenue for Colleges and Universities

by Type of Institution



Source of Data: National Center for Education Statistics, Financial Statistics of Institutions of Higher Education, Fiscal Year 1976.

for five different types of postsecondary institutions. Even within these types, there are major differences in funding patterns. The patterns and resulting funding strategies are due to a combination of differences in institutional mission and form of governance.

The financial management issues addressed by governing boards vary, depending on the funding strategy employed for the type of institution. The various revenue sources are affected differently by such factors as enrollment patterns, political climate, economic conditions, and governmental priorities. For example, a public, two-year institution depends heavily on the changing political, social, and economic factors of the local community. A private university is concerned with a different set of factors such as general economic conditions, tuition, donor relations, financial aid requirements, federal education and research priorities, and its continuing ability to recruit a desired student body.

Since environmental factors affect the revenue process differently, it is possible that one type of institution, *because of its funding sources*, can be in relatively stable financial condition while another will be adversely affected.

There are other factors of which governing boards should be aware when discussing the funding strategy of their institutions. These factors affect the flexibility, stability, and control of revenues and include:

- **"Hard" and "soft" money.** A distinction should be made between revenues that are recurring ("hard") such as tuition and appropriations and those that are nonrecurring ("soft") such as those received from grants and contracts. If an institution relies heavily on soft money to fund its long-term commitments such as tenured faculty, it has a relatively risky funding strategy. Board members should understand how stable the institution's funding is.

- **The interrelationships of revenues and expenditures.** Relationships often exist among revenues, which make the amount of one source of revenue dependent on others. For example, gifts to endowment ultimately affect endowment income, and tuition levels often depend on the amount of public funds appropriated. A second relationship is the change in expenditures because of a change in revenues, such as when an increase in tuition causes an increase in the need for financial aid. A third relationship is the change in revenues because of a change in expenditures; this may be illustrated by the cost of housing and food services, which determines the price and ultimately the revenues that are received. On the expenditure side, the governing board should differentiate between one-time and continuing expenditures, such as buying a computer or constructing a building on the one hand and paying salaries of tenured faculty or maintaining a building on the other. The one-time expenditure can often be financed from reserves or from soft money. Continuing expenditures, however, should be an integral part of the operating budget, where they are subject to frequent control and evaluation.

Given the numerous and complex responsibilities the governing board has in planning and budgeting, a natural concern is how to systematically develop a method by which the board can "carry its weight" in the process. As emphasized throughout this monograph, the board depends on the quality of the information supplied to it by the administration. A board will be better prepared and better able to respond effectively if the planning and budgeting process is developed, reviewed, and approved over several meetings.

Generalizations concerning board involvement are perhaps inappropriate because of the variety of board committees, form of governance, and frequency of meetings; however, the following case may help to illustrate effective board involvement in planning and budgeting. It illustrates the role of the board in the process and the presentation of materials to the board.

Assume a public institution with a board of eight members, which meets four times a year; there are no committees of the board.

September Meeting:

Objectives:

(a) Examine the environmental factors currently affecting the institution and how they are expected to change over the next year.

(b) Review the past financial performance of the institution by examining the annual operating reports and the external audit reports.

(c) Review the current budget and any recommended changes.

December Meeting:

Objectives:

(a) Establish the assumptions to be used for creating the financial plans and budgets. These may include inflation assumptions, estimated salary increase requirements, tuition increase, and endowment payout rate.

(b) Review the current budget and any recommended changes.

March Meeting:

Objectives:

(a) Examine the proposed plans and budgets, specifically approving (if appropriate) any new programs.

(b) Review the current budget and any recommended changes.

June Meeting:

Objectives:

(a) Approve plans and budgets based on the actions of governmental authority. Approval should include authorization for the following year's budget, salary increases, and new program offerings.

(b) Review and assess current year's financial activity.

Suggested Questions

Though the case is oversimplified, it illustrates the systematic presentation of materials to the board. The various presentations build on information previously provided to the board which, in a natural process, leads the board to the ultimate decision of approving the institution's plans and budgets. Boards meeting more frequently and having several committees have the opportunity for greater participation in the planning and budgeting process.

The next chapter more clearly describes the interrelationship of the plan, budget, and operating statements. Also, the reports in that chapter illustrate in greater detail the kinds of information and the formats that will assist governing boards in their deliberations on plans and budgets.

1. Has the governing board examined the institution's mission in comparison to its actual program activities?

2. To what extent have the institution's environmental conditions affected the long-range planning?

3. Does the board critically examine the sources of funding for new programs?

4. Has the board established a policy of having existing programs critically examined for purpose and substance?

5. To what extent has the institution's financing strategy been articulated and justified by the administration?

Implementation

Chapter 6

The preceding chapters have identified financial policy areas of concern to governing boards and have suggested ways for the administration to transmit financial data to the board. This chapter presents an approach for bringing the preceding chapters together and integrating their suggestions into a system of reporting that will enable the board to carry out its responsibilities. The basic system is described here, with illustrative formats for reports that could be provided to the board. There are also several subsets of reports, which can be used as the board's interests expand into specific areas, or as time permits, or as priorities of issues require that more detailed information be available. The basic reporting system, which should exist in every institution, is composed of the following:

1. **State of the institution** (see Report No. 1).
2. **Long-range plan and budgets** (see Report Nos. 2-11).
3. **Operating reports** (see Report Nos. 12-14).
4. **Results of operations** (see Report Nos. 15-18).
5. **External auditor's report** (see "Illustrative Exhibits").

The reports presented below for Hybrid University are based on data contained in the "Illustrative Exhibits," which follow this chapter. It is important to note that these reports only *illustrate* the principles contained in this monograph. There is no intention to imply that the formats presented are prescriptive or are preferred over other alternatives; neither are they comprehensive. Each institution's governing board and administration should determine collectively what kinds of information and what formats are appropriate for their requirements. The information should then be tested to see if it is, in fact, useful.

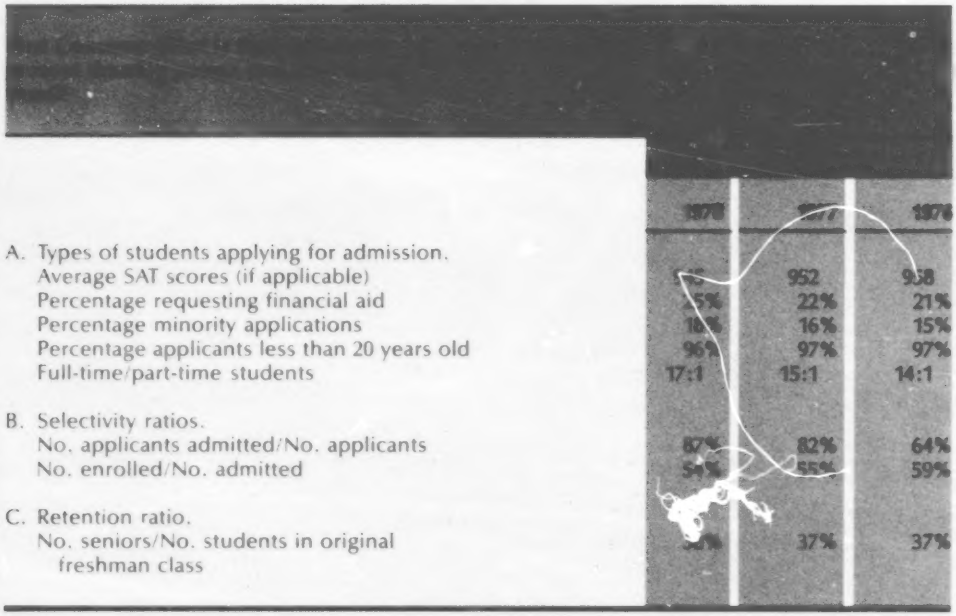
All the reports in this chapter have a specific reference point. The assumption is made that the institution is operating in the fiscal year 1978-79, and is reviewing all these reports in January. This consequently assumes that the proposed budget is for fiscal year 1979-80, that the prior year's report is for fiscal year 1977-78, and that the four years included in the long-range plan begin in 1980-81.

State of the Institution

Report No. 1. The purpose of the annual state-of-the-institution report is to provide the governing board with an overview, described in Chapter 1, that will allow it to examine change in such areas as drawing power, institutional environment, and financial health. To do so, the report must show trends; this will require at least three successive years of information. The report below, for Hybrid University, illustrates parts of one of the subjects mentioned above, namely, drawing power. Other reports should be designed to present information on additional areas.

Report No. 1
State-of-the-Institution Report
Issue: Drawing Power

Hybrid University



A. Types of students applying for admission.			
Average SAT scores (if applicable)		952	958
Percentage requesting financial aid		22%	21%
Percentage minority applications		16%	15%
Percentage applicants less than 20 years old		97%	97%
Full-time/part-time students		15:1	14:1
B. Selectivity ratios.			
No. applicants admitted/No. applicants		82%	64%
No. enrolled/No. admitted			59%
C. Retention ratio.			
No. seniors/No. students in original freshman class		37%	37%

Other concerns on the issue of drawing power could relate to state and national trends. For example, the following questions could be asked:

1. *What changes at the state and national levels are affecting drawing power?*
   a. *Kinds of students seeking admission within the state and at the national level.*
   b. *Kinds of state and federal legislation that may affect financial aid.*

2. *What are the numbers of potential students within the state and at the national level?*
   a. *Numbers of 18-year-olds at the state and national levels.*
   b. *Numbers of 18-year-olds at the state and national levels attending college.*

Long-Range Plan and Budgets

Report No. 2. As the administrators and governing board deliberate on the future of the institution, they should annually review and reaffirm its mission and goals. The statements of mission and goals need not necessarily be changed unless there has been recognition of a need for change. Reviewing the statements will help to insure that the plan and budgets are consistent with them.

The mission statement should be brief and should state in general terms the overall purpose of the institution. The statement of Hybrid University's academic goals below contains only those goals related to students and faculty, but additional statements should be prepared for such areas as individual academic programs, undergraduate and graduate education, research, public service, and student access.

Report No. 2
Statement of Mission and Goals
Hybrid University

[redacted]

Hybrid University is a small university dedicated to providing excellent educational opportunities in liberal arts, engineering, and business administration. Special emphasis is devoted to providing continuing education opportunities to residents of the nearby urban community.

[redacted]

Students. Hybrid University strives to achieve a balanced student body with strong representation of minority and women students. It is expected that regular students be full-time and that only a small fraction take less than a full load. Only students in the continuing education program are encouraged to be part-time.

Faculty. Hybrid University seeks to have an excellent teaching and research faculty and has a policy that at least 85% have a doctoral degree. The ratio of tenured faculty is closely monitored and is maintained at less than 80%. The university is also committed to seeking a balanced faculty, with special attention being given to women and minorities.

Other statements would describe individual academic programs, undergraduate and graduate education, research, public service, and student access.

Report Nos. 3 and 4. A clear statement of the environmental assumptions used to create the long-range plan and budgets provides the governing board with information on the constraints and realities in the institution's operating environment. The environmental assumptions are both external and internal, and can be considered separately for the long-range plan or can include specific assumptions such as the amount of salary increase for the budget under consideration. Depending on the type of board activities, those assumptions may be reviewed and approved by the board prior to development of the long-range plan and the current year's budget, or they may be reviewed and approved *concurrently* with approval of the budget.

Some of the external and internal assumptions used by Hybrid University are contained in Report No. 3, while selected historical data are presented in Report No. 4.

Report No. 3
Environmental Assumptions
Hybrid University

[redacted]

Economic situation. The national growth rate will be lower, perhaps negative, and inflation will remain high, at least 7%. Secular unemployment may persist. Per capita income will grow more slowly. The growth rate of the local community should continue to increase due to the shift in population to this state and to the effective utilization of its natural resources, primarily coal and water.

Construction price index. Current trends indicate an increase ranging from 7% to 9% over the present. Capital budgets have been adjusted to reflect the estimated increase in the construction index.

Alternative educational patterns, continuing education. The most pervasive influence is the decrease in traditional college-age students, the increase in older adults seeking education, and the continuing increase in the number of part-time students. The university is responding to these changing conditions with the new External Degree Program and offerings in the Division of Continuing Education, in particular the "Weekend College."

National attitude toward higher education. People are concerned about the high cost of college and by the perceived inability of collegiate training to prepare people adequately for jobs. Higher education will probably decrease in importance for funding among other social priorities such as health care and full employment.

State attitudes toward higher education. This state's residents will continue to support colleges and universities with enthusiasm. They will continue to demand more services and opportunities, and their confidence will be retained at its present high level.

State aid to independent colleges. The state's residents generally oppose use of public monies in support of independent higher education. However, state appropriations are presently being made to several independent colleges, which may gain even more support from the legislature.

Report No. 4
Environmental Assumption
Historical Data
Hybrid University

Other issues to include may be local and regional labor market trends; governmental regulations; labor union activity; national trends in tuition; and national faculty salary trends.

[redacted]

Students and Faculty. The tuition rate for 1978-79 is $1,500, with the expectation that it will rise to $2,000 for the academic year 1983-84—a compound annual growth rate of 6%. For this same period, FTE enrollment is expected to drop from 1,846 to 1,725 due to the expected decline in the number of 18-year-olds.

Size of the faculty is also expected to decline during this period, from 122 to 92, with most of the decrease due to retirements and turnover.

The need for financial aid continues. With fewer students able to pay full tuition, the student aid budget will rise at a rate of 2% to 4% above the general rate of inflation. However, current and proposed federally sponsored aid programs should cover much of the increased costs. Currently, institutionally based aid is $200,000, which is allocated among 465 students. It is estimated that by 1983-84 the aid requirement will increase to $255,000 for the same number of students.

Faculty compensation will continue to increase regularly in order for the institution to maintain a competitive position with the compensation of peer institutions. Increases in insurance premiums and social security taxes are raising the cost of benefits at a rate greater than that of general inflation. Special attention should be given to the salaries of junior faculty, which have fallen behind the national average for this type of institution. Compensation to the faculty is currently $3.196 million and is anticipated to increase to $3.532 million in 1983-84. Or stated another way, average faculty compensation will grow from $26,200 to $38,400 by 1983-84, a compound annual increase of 8%.

With regard to unionization, unless enabling legislation is passed by the state legislature, it is unlikely that union influence will increase. On the other hand, if new laws are enacted, it is possible that union activity will increase.

Additional material would be appropriate for:
- *Description of, justification for, and cost effect of changes in academic and support programs.*
- *Analysis of trends for executive, professional, technical, and clerical staffs.*
- *Special descriptions of items having major effect on the plan and operating budgets, such as fund-raising campaigns, new bond issues, appropriation expectations, library acquisitions, computing needs, utilities, and plant fund transfers.*

[redacted]

	Percentage of original freshman class at Hybrid University who return as		
Graduation Class of	Sophomores	Juniors	Seniors
1976	79.0	61.6	38.7
1977	79.7	64.1	36.8
1978	80.0	65.8	37.0
1979	84.8	68.2	38.0
1980	83.2	66.6	
1981	82.1		

[redacted]

Year	Tuition	Percentage Increase	Cost-of-Living Increase
1975-76	$1,200	—	10.1%
1976-77	1,300	8.3%	7.9
1977-78	1,400	7.7	6.3
1978-79	1,500	7.1	(est.) 7.0

[redacted]

	A	B	C	D	E
Year	Applied	Admitted	Matriculated	(B/A)	(C/B)
1974-75	1,667	1,250	650	.75	.52
1975-76	1,655	1,059	625	.64	.59
1976-77	1,364	1,118	615	.82	.55
1977-78	1,341	1,167	630	.87	.54

Historical data used depend largely on the environmental assumptions selected for emphasis. Logical items might include:

- *Tuition by sector (public and independent) and type of institution (such as Carnegie classification).*
- *Source of income.*
- *Salary survey information.*
- *Student/faculty ratio.*
- *Tenured/total faculty ratio.*
- *Educational and general expenditures per student.*
- *Enrollments by sector (public and independent) and type of institution (such as Carnegie classification).*

Report Nos. 5-11. The long-range plan provides the governing board with (1) information to assist it in evaluating the financial feasibility of the mission and goals, (2) information to evaluate the validity of the financially related policies it has approved, and (3) a framework for future decision making. In this context, the operating budget provides the opportunity for the board to (1) review and approve the acquisition and allocation of financial resources and (2) determine that proposed revenues and expenditures are compatible with the long-range plan.

The operating budget and long-range plan should be prepared annually (if the institution is on a biennial appropriation, frequency may be every two years), and should be based on three to five years of historical data. For certain types of information, such as gifts from private sources, longer trendlines may be appropriate. The long-range plan should contain projections for at least four years, the operating budget for the coming year, and the capital budget for the coming year as well as estimated cash flows for several succeeding years.

The presentation of the operating budget and long-range plan to the governing board is illustrated in Report Nos. 5-11. The first of these, No. 5, is the primary report, which is highly aggregated, showing general information and the assumptions used in preparing the operating budget and long-range plan (see Part A), estimated current funds revenues (see Part B), and estimated current funds expenditures and transfers (see Part C). Revenues are listed by source and expenditures are listed by function to match the format of the year-end statements.

The aggregated amounts are supported by more detailed reports, which include (in Report Nos. 6-9) revenue estimates for tuition and fees, endowment, gifts, and auxiliary enterprises; expenditures and transfers are supported by a report (No. 10) for academic and support departments. All these reports include information for the budget year under consideration and for future years, in appropriate detail for the board to understand the major components of revenue and expenditure. Projecting for future years, instead of presenting only the budget year under consideration, enables the board to identify the potential effect of its current decisions.

With this information the board now has an understanding of the external factors affecting the institution, the internal assumptions made by the institution, a review of the prior year's expenditures, a projection of the current year's expenditures, the budget for the coming year (with a detailed development of revenues and expenditures), and projected plans for four additional years. This should give the board basic information with which to approve the budget, which is an expression in financial terms of the plans for operating the institution in the coming year. During this process the governing board must decide the following:

- Tuition rate.
- Total amount available for compensation increases.
- Endowment payout rate.
- Amount to set aside for plant purposes.
- Changes in existing academic programs.

The capital budget (Report No. 11) is normally prepared at the same time as the annual operating budget, but because of the different focus—on capital needs—it is presented and reviewed separately.

Report No. 5
Operating Budget and Long-Range Plan

Hybrid University
A. General Information

Item	Actual 1977-78	Projected 1978-79	Proposed Budget 1979-80	Plan 1980-81	Plan 1981-82	Plan 1982-83	Plan 1983-84	Supporting Report No.
Students and faculty								
Tuition rate	$ 1,400	$ 1,500*	$ 1,600	$ 1,700	$ 1,800	$ 1,900	$ 2,000	6
Total enrollment (head count)	1,935	1,960*	1,970	1,934	1,928	1,905	1,883	
FTE enrollment	1,841	1,846*	1,850	1,825	1,790	1,750	1,725	6
FTE faculty	118	122*	115	110	104	98	92	
Student-faculty ratio (based on FTEs)	15:1	15:1*	16:1	17:1	17:1	18:1	19:1	
Number of students receiving degrees	230	225	250	240	240	230	240	
Number of students receiving financial aid	465	465*	465	465	465	465	465	
Average institutionally-based aid per FTE student	$51	$57*	$57	$60	$64	$68	$74	
Percentage increase	—	11.8%	0%	5.3%	6.7%	6.3%	8.8%	
Faculty compensation (total, in thousands)	$ 3,007	$ 3,196	$ 3,250	$ 3,366	$ 3,432	$ 3,488	$ 3,532	
Average faculty compensation	$24,200	$26,200	$28,300	$30,600	$33,000	$35,600	$38,400	
Percentage increase	—	8.0%	8.0%	8.0%	8.0%	8.0%	8.0%	
Staff								
Professional and administrative (FTE)	32	34*	35	36	36	36	36	
Clerical (FTE)	69	72*	76	77	72	72	72	
Other (FTE)	32	36*	36	36	36	36	36	
Student employees (FTE)	40	44*	42	40	40	40	40	
Total staff salaries, wages, and benefits (thousands)	$ 1,686	$ 1,960	$ 2,259	$ 2,291	$ 2,460	$ 2,631	$ 2,817	
Average staff salaries								
Professional and administrative	$18,700	$20,000	$21,400	$22,900	$24,700	$26,400	$28,200	
Clerical	9,200	9,900	10,600	11,300	12,100	12,900	13,800	
Other	13,300	14,200	15,200	16,300	17,400	18,650	20,000	
Students	1,250	1,375	1,500	1,660	1,830	2,010	2,215	
Endowments and quasi-endowments								
Market value (thousands)	$15,500	$17,300	$18,335	$19,645	$21,367	$23,271	$25,285	7
Yield on market value	3.7%	4.0%	4.0%	4.0%	4.0%	4.0%	4.0%	7
Gifts (thousands)								
Current fund	$ 1,220	$ 1,300	$ 1,400	$ 1,500	$ 1,600	$ 1,700	$ 1,800	8
Endowment and similar funds	2,300	400	675	800	925	1,050	1,175	8
Plant fund	195	190	280	350	500	650	800	8
Student loan fund	100	110	115	120	125	130	135	8
Plant and equipment								
Book value (thousands)	$41,600	$42,000	$42,500	$43,100	$43,600	$44,400	$45,000	
Square feet	380,000	380,000	380,000	380,000	380,000	380,000	380,000	

*Actual fall 1978 figures. Note: This is a sample list; it is not intended to be all-inclusive.

Report No. 5
Operating Budget and Long-Range Plan

Hybrid University

B. Revenues (thousands)

Item	Actual 1977-78	Projection 1978-79	Proposed Budget 1979-80	Plan	Plan	Plan	Plan	Supporting Report No.
Tuition and fees	$ 2,600	$ 2,838	$ 3,080	$ 3,243	$ 3,382	$ 3,505	$ 3,650	6
Federal appropriations	500	525	550	575	600	625	650	
State appropriations	700	700	700	700	700	700	700	
Local appropriations	100	105	110	115	120	125	130	
Federal grants and contracts	395	380	390	400	405	410	420	
State grants and contracts	35	20	—	—	—	—	—	
Local grants and contracts	30	15	—	—	—	—	—	
Private gifts, grants, and contracts	1,230	1,300	1,400	1,500	1,600	1,700	1,800	8
Endowment income	534	692	740	794	870	953	1,030	7
Sales and services of educational activities	190	200	210	220	230	240	250	
Other sources	40	—	—	—	—	—	—	
Subtotal	6,354	6,775	7,180	7,547	7,907	8,258	8,630	
Auxiliary enterprises	2,200	2,300	2,400	2,500	2,600	2,700	2,800	9
Total	8,554	9,075	9,580	10,047	10,507	10,958	11,430	
Percentage increase		6.1%	5.6%	4.9%	4.6%	4.3%	4.3%	
Breakdown by type of revenue								
Unrestricted	7,460	7,926	8,374	8,781	9,177	9,562	9,963	
Restricted	1,094	1,149	1,206	1,266	1,330	1,396	1,467	

Revenue categories may be detailed as needed.

Report No. 5
Operating Budget and Long-Range Plan

Hybrid University

C. Current Funds Expenditures and Transfers (thousands)

Item	Actual 1977-78	Budget 1978-79	Proposed Budget 1979-80	Plan 1980-81	Plan 1981-82	Plan 1982-83	Plan 1983-84	Supporting Report No.
Expenditures and mandatory transfers								
Educational and general								
Instruction	$3,498	$3,740	$3,835	$4,088	$4,345	$4,620	$4,920	10
Research	500	435	480	510	520	535	550	10
Public service	155	160	175	185	195	205	220	10
Academic support	250	260	270	285	295	305	315	10
Student services	200	210	215	225	235	245	255	10
Institutional support	490	470	495	520	545	575	605	10
Operation and maintenance of plant	220	255	280	295	305	440	510	10
Scholarships and fellowships	190	200	220	230	240	240	255	10
Mandatory transfers	192	192	192	192	192	192	192	10
Subtotal	5,605	5,830	6,177	6,540	6,832	7,357	7,822	9
Auxiliary enterprises	2,150	2,280	2,220	2,370	2,515	2,710	2,905	
Total expenditures and mandatory transfers	7,756	8,130	8,397	8,914	9,472	10,067	10,727	
Percentage increase		4.8%	3.3%	6.2%	6.3%	6.3%	6.6%	
Nonmandatory transfers & additions (deductions)								
Unrestricted gifts allocated to other funds	(650)	(600)	(800)	(850)	(800)	(900)	(900)	
Portion of quasi-endowment gains appropriated	40	—	—	—	—	—	—	
Other	25	—	—	—	—	—	—	
Increase (decrease) of net revenues	213	145	383	333	235	91	(97)	

Expenditure categories may be detailed as needed.

Report No. 6
Projected Enrollment and Income from Tuition and Fees

Hybrid University

Enrollment (FTE)

Year	Freshman	Sophomore	Junior	Senior	Continuing Education	Total
1973-74*	630	490	391	242	18	1,771
1974-75*	646	502	382	238	26	1,794
1975-76*	619	517	404	240	30	1,810
1976-77*	625	525	425	232	28	1,835
1977-78*	630	520	422	239	30	1,841
1978-79*	645	517	416	235	33	1,846
1979-80	645	500	411	258	36	1,850
1980-81	645	490	400	252	38	1,825
1981-82	618	498	385	248	41	1,790
1982-83	596	478	393	240	43	1,750
1983-84	571	470	386	252	46	1,725

	1979-80	1980-81	1981-82	1982-83	1983-84
Enrollment (FTE)	1,850	1,825	1,790	1,750	1,725
Tuition rate	$1,600	$1,700	$1,800	$1,900	$2,000
Total tuition	$2,960,000	$3,102,500	$3,222,000	$3,325,000	$3,450,000
Student activity fees	$ 20,000	$ 20,000	$ 20,000	$ 20,000	$ 20,000
Summer school	100,000	120,000	140,000	160,000	180,000
Total tuition and fee income	$3,080,000	$3,242,500	$3,382,000	$3,505,000	$3,650,000
Percentage increase		5.3%	4.3%	3.6%	4.1%

*Data for prior years provided to show enrollment trends.

Report No. 7
Projected Income from Endowment and Quasi-Endowment Funds

Hybrid University

	1979-80	1980-81	1981-1982	1982-83	1983-84
Pooled Investments					
Total units	1,047,500	1,074,650	1,115,990	1,162,990	1,211,240
Unit value	$16.55	$17.35	$18.25	$19.15	$20.10
Earnings per unit	$.66	$.69	$.73	$.77	$.80
Yield on market value	4.0%	4.0%	4.0%	4.0%	4.0%
Endowment (in thousands)					
Principal (market)	$11,055	$12,290	$13,727	$15,304	$17,004
Income	440	489	549	615	679
Term Endowment					
Principal (market)	3,260	2,689	2,683	2,815	2,874
Income	130	107	107	113	114
Quasi-Endowment					
Principal (market)	3,020	3,666	3,957	4,152	4,408
Income	120	146	158	167	175
Separately Invested					
Term Endowment					
Principal (market)	200	200	200	200	200
Income	10	10	10	10	10
Quasi-Endowment					
Principal (market)	800	800	800	800	800
Income	40	42	46	48	52
Total market value	$18,335	$19,645	$21,367	$23,271	$25,286
Percentage increase over prior year		7.1%	8.8%	8.9%	8.7%
Total income for budget	$740	$794	$870	$953	$1,030
Percentage increase over prior year		7.3%	9.6%	9.5%	8.1%

Report No. 8
Projected Private Gifts, Grants, and Contracts
(in thousands)
Hybrid University

	1979-80	1980-81	1981-82	1982-83	1983-84
By Fund Group					
Current					
Unrestricted	$1,000	$1,050	$1,100	$1,150	$1,200
Restricted	400	450	500	550	600
Endowment and similar					
Unrestricted	450	500	550	600	650
Restricted	150	200	250	300	350
Annuity and life income	75	100	125	150	175
Student loan	115	120	125	130	135
Plant	200	350	500	650	800
Total	$2,390	$2,770	$3,150	$3,530	$3,910
Percentage increase		15.9%	13.7%	12.1%	10.8%
By Type of Donor					
Individuals					
Alumni	$1,190	$1,495	$1,800	$2,105	$2,410
Non-alumni	400	425	450	475	500
Bequests	100	100	100	100	100
Corporations	250	275	300	325	350
Foundations	450	475	500	525	550
Total	$2,390	$2,770	$3,150	$3,530	$3,910

Report No. 9
Projected Auxiliary Enterprise Income

(in thousands)
Hybrid University

	1979-80	1980-81	1981-82	1982-83	1983-84
Residence Halls					
Income	$1,295	$1,326	$1,341	$1,360	$1,375
Expense	825	891	961	1,039	1,128
Mandatory transfers					
Debt service	250	250	250	250	250
Renewals and replacements	70	70	70	70	70
Net	150	115	60	1	(73)
Food Services					
Income	1,025	1,090	1,170	1,245	1,325
Expense	1,000	1,080	1,170	1,263	1,365
Net	25	10	—	(18)	(40)
Other Services					
Income	80	84	89	95	100
Expense	75	79	84	88	92
Net	5	5	5	7	8
Total income	$2,400	$2,500	$2,600	$2,700	$2,800
Total expense	1,900	2,050	2,215	2,390	2,585
Total mandatory transfers	320	320	320	320	320
Total expense and mandatory transfers	2,220	2,370	2,535	2,710	2,905
Net	180	130	65	(10)	(105)
[illegible]					
Room	$ 850	$ 885	$ 910	$ 940	$ 965
Board	650	700	760	820	885
Total	$1,500	$1,585	$1,670	$1,760	$1,850
Percentage increase	—	5.7%	5.4%	5.4%	5.1%
[illegible]					
Number of residents	1,525	1,500	1,475	1,450	1,425
Number of food service contracts	1,575	1,560	1,540	1,520	1,500
Design capacity	1,650	1,650	1,650	1,650	1,650
Occupancy rate	92%	91%	89%	88%	86%

Report No.10
Estimated Expenditures and Mandatory Transfers

for Academic and Support Departments
(in thousands)
Hybrid University

Educational and General	1979-80	1980-81	1981-82	1982-83	1983-84	Compound Growth Rate
Instruction						
Business Administration	$1,070	$1,165	$1,265	$1,370	$1,480	
Continuing Education	595	625	650	680	715	
Engineering	865	900	945	985	1,035	
Liberal Arts	1,105	1,180	1,265	1,355	1,450	
Other	200	210	220	230	240	
Total	3,835	4,080	4,345	4,620	4,920	5%
Research						
Business Administration	255	270	280	295	310	
Continuing Education	40	40	40	40	40	
Engineering	200	200	200	200	200	
Total	495	510	520	535	550	3%
Public Service						
Business Administration	145	150	160	165	175	
Continuing Education	30	32	35	40	45	
Total	175	182	195	205	220	3%
Academic Support	270	280	290	305	315	2%
Student Services	215	225	235	245	255	4%
Institutional Support	495	520	545	575	605	5%
Operation and Maintenance of Plant	290	335	385	440	510	15%
Scholarships and Fellowships	210	220	230	240	255	5%
Total expenditures	5,985	6,352	6,745	7,165	7,630	6%
Mandatory Transfers						
Principal and Interest	90	90	90	90	90	
Renewals and Replacements	100	100	100	100	100	
Loan Fund Matching Grant	2	2	2	2	2	
Total mandatory transfers	192	192	192	192	192	0%
Total expenditures and mandatory transfers	6,177	6,544	6,937	7,357	7,822	6%
Percentage increase		5.9%	6.0%	6.1%	6.3%	

Report No. 11
Capital Budget

(in thousands)
Hybrid University

	Estimated Completion Date	Estimated Project Cost	Cash Flow: To Date	Cash Flow: Current Year	Cash Flow: Proposed for Budget Year
Projects Under Construction					
Renovation—Olde Hall	Apr 1980	$ 3,250	$2,175	$ 750	$ 325
Renovation—Gnew Dorm	Aug 1981	750	125	325	175
Renovation—Steam Plant	Dec 1983	1,975	350	175	250
		$ 5,975	$2,650	$1,250	$ 750
Fund Sources					
State Grants		4,225	1,985	100	1,165
Federal Grants		225	100	100	25
Note Payable*		1,000	1,000	—	—
Gifts		250	175	50	25
Plant Fund Reserves		275	200	50	—
		$ 5,975	$3,460	$ 300	$1,215
Cumulative Net Cash Flow			+$ 810	−$ 140	+$ 325
Proposed Projects					
Renovation—Thomas Hall	Aug 1983	$ 4,250			$1,450
Renovation—Richards Gym	Apr 1984	2,850			750
Renovation—Harrison Quad	Sep 1985	6,550			250
		$13,650	$ -0-	$ -0-	$2,450
Fund Sources					
State Grants		$ 1,000		$ -0-	$ 250
Federal Grants		500		-0-	100
Bond Payable		7,500		2,500	2,500
Gifts		2,000		750	750
Plant Fund Reserves		2,650		800	800
		$13,650		$4,050	$4,400
Cumulative Net Cash Flow for Proposed Projects				+$4,050	+$6,000
Projects Authorized for Future Consideration					
Chilled-Water System		$ 3,500			
Fire Station		1,250			
Renovation—Alpine Hall		5,250			
Renovation—Zephyr Wing		2,800			
		$12,800			

Payable from residence hall revenues.

Supporting this report would be the detail for funding sources of each project, a description of the status of projects under construction, and a description and justification for proposed projects.

Report No. 12
Statement of Operations and Variance Analysis

Six Months Ended December 31, 1978
(in thousands)
Hybrid University

Operating Reports

Report Nos. 12-14. Once all budgets are approved, the institution is able to move forward and operate, but it is still necessary that the board have periodic reviews during the year of actual performance relating to the plan. Such reviews can be based on a series of statements of operations and variance analyses. Although frequency would depend on board preference, differences in institutional requirements, and number of board meetings, these reports would normally be presented quarterly, but if the executive committee or finance committee meets monthly, they may be presented monthly. These reports enable the board to be kept informed on whether the plan, as reflected in the annual budget, is being followed.

The purpose of the statement of operations and variance analysis (Report No. 12) is to provide the governing board with the opportunity to (1) review the financial operations of the institution, (2) assure itself that the budget is being followed, and (3) see that variances are analyzed and documented. The statement should contain the original budget approved by the board, estimate of actual performance for the year, and expected variance. As in Report No. 5, revenues are listed by source and expenditures are listed by function.

The next two reports, "Development Program" and "Investment Performance" (Report Nos. 13 and 14), are examples of reports that supplement the statement of operations and variance analysis. Such reports can be designed for other revenue sources as well as for expenditures; the amount of detail would depend on board preference.

	Jul 1–Dec 31		Year 1978-79		Variance	Reference
	Budget	Actual	Budget	Projection		
Revenues						
Tuition and fees	$1,375	$1,395	$2,800	$2,838	$ 38	A
Federal appropriations	260	245	525	525	—	
State appropriations	350	365	700	700	—	
Local appropriations	55	40	105	105	—	
Federal grants and contracts	190	200	380	380	—	
State grants and contracts	10	8	20	20	—	
Local grants and contracts	10	12	15	15	—	
Private gifts, grants, and contracts	800	1,000	1,150	1,300	150	B
Endowment income	360	340	725	692	(33)	C
Sales and services of educational activities	100	100	200	200	—	
Subtotal	3,510	3,705	6,620	6,775		
Expenditures and Mandatory Transfers (Educational and General)						
Instruction	1,825	1,835	3,670	3,690	20	A
Research	245	255	485	485	—	
Public service	85	87	168	168	—	
Academic support	130	128	260	260	—	
Student services	105	110	210	210	—	
Institutional support	235	230	470	470	—	
Operation and maintenance of plant	110	130	225	255	30	D
Scholarships and fellowships	100	125	190	200	10	A
Mandatory transfers, educational and general	100	100	192	192	—	
Subtotal	2,935	3,000	5,870	5,930	60	
Excess (deficit)	575	705	750	845	95	
Auxiliary enterprise revenues	1,110	1,160	2,225	2,300	75	A
Auxiliary enterprise expenditures and mandatory transfers	1,075	1,100	2,150	2,200	50	A
Excess (deficit)	35	60	75	100	25	
Nonmandatory transfers	400	400	800	800	—	
Excess (deficit)	$ 210	$ 365	$ 25	$ 145	$120	

The above format is intended to be representative only of the principle that governing boards should be aware of how actual results compare to the budget and of the reasons for major variances. Many other report formats and financial information accomplish the same purpose. Comparison with prior years, use of percentage analysis, and analysis by responsibility center are some of the more frequently used methods for advising the board of actual performance.

Report No. 12 (cont.)
Explanation of Variances

Hybrid University

Reference	
A Tuition and fees	**+$37,500**
Instruction	**+ 20,000**
Scholarships and fellowships	**+ 10,000**
Auxiliary enterprises	
Revenues	**+ 75,000**
Expenditures	**+ 50,000**

Tuition income for the fall term is $20,000 above the estimate, due to an actual student enrollment that was greater than anticipated. The original fall enrollment projection was 1,800 FTE; actual enrollment was 1,846. Based on the higher enrollment, it is projected that winter- and spring-quarter enrollments will also increase slightly, causing a total variance of $37,500. In addition, part-time instructors were hired ($20,000) and scholarships awarded ($10,000) due to increased enrollments.

The increase in auxiliary enterprise revenues and expenditures is also due to the increased number of students.

B Private gifts, grants, and contracts **+$150,000**

The university received in December an anonymous gift. The gift is unrestricted and a recommendation for its use will be made at the March 1979 board meeting.

C Endowment income **−$33,000**

The original budget estimate projected a yield of 4.5 percent; the current projection is that it will be closer to 4 percent of market value. This will create a downward adjustment of approximately $33,000.

D Operation and maintenance of plant **+$30,000**

The increase in rates by the local utility, coupled with the severe winter, caused an increase in the electricity bill. The total increase is estimated at $30,000.

Report No. 13
Development Program

Summary Report for the Six Months
Ended December 31, 1978
(in thousands)
Hybrid University

	1977-78 Total	1978-79 Goal	Amount Received This Six-Month Period	Amount Received Same Six-Month Period Last Year
Source				
Individuals				
Alumni	$ 785	$ 700	$ 550	$ 645
Non-alumni	275	300	200	175
Foundations	390	425	210	190
Corporations	215	225	115	105
Bequests	2,150*	100	375	1,750*
Total	$3,815	$1,750	$1,450	$2,865
Purpose				
Current				
Unrestricted	$ 370	$ 150	$ 300	$ 200
Restricted	850	900	700	600
Student loan	100	110	50	20
Endowment	2,300*	400	250	1,985*
Plant	195	190	150	60
Total	$3,815	$1,750	$1,450	$2,865

The annual alumni fund drive is expected to achieve its goal for the year. Giving from foundations and business corporations is as anticipated. The receipt of a $150,000 gift from an anonymous donor in December is expected to place total giving from all donors for the year in excess of the goal.

**Includes bequest of $1.6 million from estate of anonymous donor.*

Report No. 14
Investment Performance

(in thousands)
Hybrid University

Types of Investments	Dec. 31, 1978		Dec. 31, 1977	
	Market Value	Percent	Market Value	Percent
Common stocks	$10,100	45	$ 7,455	43
Municipal bonds	1,800	8	1,875	11
Short-term investments	700	3	500	3
Other corporate notes and bonds	7,200	32	6,700	39
U.S. government obligations	220	1	200	1
Real estate	630	3	550	3
Mortgage notes receivable	1,800	8	—	—
Total	$22,450	100	$17,280	100

Market Values and Income per Unit		
Date	Market Value	Income
December 31, 1978	$15.75	$.62
June 30, 1978	15.00	.56
December 31, 1977	13.75	.52

Summary of Investment Performance	Year Ended December 31, 1978		
	Rate of Yield	Market Price Change	Total Return
Pooled Endowment Funds	3.9%	14.5%	18.4%

This is representative of only some of the information important for examining investment performance. Refer to NACUBO's booklet "Reporting on Investments of Endowment Funds" and to the annual "NACUBO Comparative Performance Study and Investment Questionnaire" for further information.

Results of Operations

Report Nos. 15-18. After being presented with the long-range plan, budget for the year, and operating reports, the board needs at the end of the year to be informed of results of operations. The statements are similar to and consistent with those prepared in accordance with generally accepted accounting principles, but have been modified for presentation to the board; the modification is designed to help the board in its review of operations for the year. As well as being a review of the year's operations, this can also be the first step in understanding the institution's finances as the board moves into the next year, in which the cycle of updating the assumptions and long-range plan and of preparing a new annual budget will occur.

The governing board must assure itself that resources entrusted to it are (1) under adequate control, (2) prudently managed, and (3) either protected or expended in accordance with the requirements of the initial providers. The board also has the responsibility of reconciling obligations made in the past with present needs as well as future requirements. The annual financial reports provide useful information for carrying out these responsibilities. At least two fiscal years should be covered by these annual reports, the most current and the one previous.

The authoritative references recommend three such reports: balance sheet, statement of changes in fund balances, and statement of current funds revenues, expenditures, and other changes. The first two of these appear as Exhibits A and B in Chapter 4 and are repeated, with the third statement, in the "Illustrative Exhibits" following the present chapter. Report Nos. 15 and 16 are similar to Exhibits A and B, but are abbreviated to illustrate their purpose; also, they may possibly be easier for trustees to read. In addition, two other reports are suggested: a statement of current fund expenditures and a statement of historical changes in fund balances (see Report Nos. 17 and 18). It should be noted that no attempt

is made in this explanation to include the accompanying notes to the financial statements; these will be found in the "Illustrative Exhibits" following this chapter.

Balance Sheet. This statement shows the assets, liabilities, and accumulated balances on a given date for each of the four funds described (see Report No. 15). It serves the same purpose as a corporate balance sheet; information on debt, working capital, and fund balances can indicate whether the institution is financially healthy. An important distinction of this balance sheet compared to a corporate balance sheet is the separation of fund balances into the groups described above. As with the Statement of Changes in Fund Balances, totals are provided for both the current and prior years.

Statement of Changes in Fund Balances. This statement (Report No. 16) shows how the financial activity for the year has affected each of the fund groups: current, student loan, endowment and similar, and plant. It addresses three primary issues discussed in this monograph:

- How were the financial resources generated?
- How were they spent?
- How were they managed and protected?

The statement is divided into three sections, each providing an answer to the above questions:

The *revenues and other additions* section brings together all the financial resources received by the institution and classifies them by purpose (fund) and restriction. The resources are also grouped according to source, such as students, appropriations, etc.

The *expenditures and other deductions* section summarizes how the financial resources were spent from each of the fund groups. A more detailed analysis of the current fund expenditures is provided in the Statement of Current Funds Expenditures (Report No. 17).

The *other changes* section shows how the financial resources were managed and protected. It is here that the fund balances are adjusted in accordance with actions taken by the governing board to reflect the institution's financial condition. For example, if the institution had to pay for current operations from funds the board had previously designated as quasi-endowment, a transfer would be shown *from* endowment and similar funds *to* current funds. Conversely, if the governing board were in a position to save or invest current revenues for the future, a transfer would be made *from* current funds *to* endowment and similar funds. A similar transfer is made when the board decides to spend current revenues for a new building or major renovation. In this case, a transfer is made *from* current funds *to* plant funds—unexpended. By closely examining the transfers and ending fund balances, trustees can see the net effect of their prior decisions on the financial status of the institution.

The Statement of Changes in Fund Balances concludes by showing the net increase or decrease in each fund group and the balances at the end of the year. The fund groups may be totaled and compared with the total amounts from the prior year, as they are in Report No. 15.

Statement of Current Funds Expenditures. This statement shows expenditures for the three subheadings in the current funds column: unrestricted—not designated, unrestricted—designated, and restricted (see Report No. 17). Expenditures are grouped by function or program activity (instruction, research, public service, etc.), with these first three functions further subdivided into academic units.

Statement of Historical Changes in Fund Balances. This statement provides an historical perspective of the financial status of the institution by displaying fund balances for five years for each fund group (see Report No. 18). This provides an important context for evaluating the present financial status of the institution.

Report No. 15

Balance Sheet

June 30, 1978
with comparative figures at June 30, 1977
(in thousands)
Hybrid University

	Current	Loan	Endowment & Similar	Plant	Total Current Year	Total Prior Year
Current assets						
Cash	$ 405			$ 75	$ 480	$ 210
Investments	680				680	520
Accounts receivable	205				205	330
Inventories and prepaid expenses	190				190	160
(Due to) Due from other funds	(80)	$ 3		155		
Subtotal	1,400	3		230	1,631	1,170
Current liabilities						
Accounts payable and accrued liabilities	350			10	360	310
Unearned (deferred) revenue	30				30	25
Portion of long-term debt due within one year	220			220	440	440
Deposits held in custody for others	100				100	75
Subtotal	700			230	930	850
Net current assets	700	3			701	320
Long-term assets						
Cash	5		170	250	425	300
Investments	350		16,250	1,000	17,600	16,100
Loans receivable	550				550	500
Deposits with trustees				200	200	200
Land, buildings, and equipment				41,650	41,650	39,000
Subtotal	905		16,420	43,100	60,425	56,100
Long-term liabilities						
Annuities payable			2,155		2,155	2,250
Notes, bonds, and mortgages payable				3,670	3,670	3,890
Subtotal			2,155	3,670	5,825	6,140
Net long-term assets	905		14,265	39,430	54,600	49,960
Net assets	$1,605	$ 3	$14,265	$39,430	$55,301	$50,280
Fund balances						
Unrestricted—not designated	500				500	490
Unrestricted—designated	143	150		550	843	780
Restricted	446	403		1,210	2,139	2,980
U.S. government grants refundable		50			50	30
Endowment			7,800		7,800	6,740
Term endowment			3,840		3,840	3,420
Quasi-endowment						
Unrestricted			1,000		1,000	850
Restricted			1,360		1,360	1,060
Annuity and life income			3,225		3,225	2,950
Investment in plant				38,210	38,210	36,540
Total fund balances	$1,605	$ 3	$17,225	$39,970	$57,803	$55,370

Report No. 16

Statement of Changes in Fund Balances

Year Ended June 30, 1978
with comparative figures at June 30, 1977
(in thousands)
Hybrid University

Current Unrestricted						Endowment and Similar	Plant		Total		Percentage Change
Not Designated	Designated	Restricted	Total		Student Loans		Unexpended	Invested in Plant	Current Year	Prior Year	
				Revenues and other additions							
$2,600	$2,200	$	$4,800	Students	$	$	$	$	$ 4,800	$ 4,400	9.1
1,300			1,300	Appropriations			50		1,350	1,340	.1
35		500	535	Government grants and contracts	18				553	535	3.4
850		370	1,220	Private gifts, grants, and contracts	100	2,300	180	15	3,815	3,525	8.2
325		224	549	Investments	23	169	35		776	715	8.5
190			190	Sales and services					190	195	2.6
40			40	Expired term endowment and other sources		10	53		103	3	N/A
5,340	2,200	1,094	8,634	**Total revenues and other additions**	141	2,479	318	15	11,587	10,713	8.2
				Expenditures and other deductions							
4,400	1,830	1,049	7,279	Operating expenditures					7,279	7,100	2.5
				Plant expenditures			1,500		1,500	1,200	25.0
				Retirement of debt			220		220	210	4.8
				Interest on indebtedness			190		190	200	5.0
		20	20	Expired term endowment and other	12	175	1		208	75	N/A
4,400	1,830	1,069	7,299	**Total expenditures and other deductions**	12	175	1,911		9,387	8,585	7.0
				Other changes							
				Additions to plant facilities				1,770	1,770	1,450	22.1
				Disposals and retirements				(115)	(115)	(125)	(8.0)
				Mandatory transfers							
	(340)		(340)	Principal and Interest			340				
(170)			(170)	Renewals and replacements			170				
(2)			(2)	Loan fund matching requirement	2						
				Nonmandatory transfers							
(700)	50		(650)	Unrestricted gifts allocated	50	550	50				
40			40	Quasi-endowment investment gains allocated		(40)					
(832)	(290)		(1,122)	**Total other changes**	52	510	500	1,655	1,655	1,325	24.9
100	80	25	213	Net increase (decrease) for the year	181	2,814	(1,033)	1,670	3,845	3,253	
400	55	421	876	Fund balance at beginning of year	502	14,406	2,793	3,654	55,117	51,864	
$ 500	$ 135	$ 446	$1,089	**Fund balance at end of year**	$683	$17,220	$1,760	$5,324	$58,962	$55,117	

Report No. 17

Statement of Current Funds Expenditures

Year Ended June 30, 1978
(in thousands)
Hybrid University

	Unrestricted					
	Not Designated	Designated	Restricted	Total	Prior Year Total	Percentage Change
Educational and General						
Instruction						
Business Administration	$ 885		$ 34	$ 919	$ 890	3.3
Continuing Education	425		125	550	570	(3.5)
Engineering	575		230	805	755	6.6
Liberal Arts	965		25	990	930	6.5
Other	110		75	185	155	19.4
Total	2,960		489	3,449	3,300	4.5
Research						
Business Administration	100		125	225	190	18.4
Continuing Education			40	40	35	14.3
Engineering			235	235	325	(27.7)
Other					100	—
Total	100		400	500	650	(23.1)
Public Service						
Business Administration	130			130	110	18.2
Continuing Education			25	25	65	(61.5)
Total	130		25	155	175	(11.4)
Academic Support	250			250	225	11.1
Student Services	200			200	195	2.6
Institutional Support	450			450	445	1.1
Operation and Maintenance of Plant	220			220	200	10.0
Scholarships and Fellowships	90		100	190	180	5.6
Total Educational and General Expenditures	4,400		1,014	5,414	5,370	.8
Auxiliary Enterprises Expenditures		1,830		1,830	1,730	5.8
Total Expenditures	$4,400	$1,830	$1,014	$7,244	$7,100	2.0

Report No. 18

Statement of Historical Changes in Fund Balances

(in thousands)
Hybrid University

	1973-74	1974-75	1975-76	1976-77	1977-78
Current					
Unrestricted—not designated	$ 800	$ 600	$ 450	$ 400	$ 500
Unrestricted—designated	110	80	85	55	143
Restricted	350	460	375	421	446
	1,260	1,140	910	876	1,089
Loan					
Designated	85	95	100	100	150
Restricted	325	344	350	369	483
U.S. government grants refundable	10	15	25	33	50
	420	454	475	502	683
Endowment and Similar					
Endowment	6,180	6,320	6,510	6,740	7,800
Term endowment	4,900	6,200	4,100	3,420	3,840
Quasi-endowment					
Unrestricted	625	650	700	800	1,000
Restricted	75	150	300	941	1,360
Annuity and life income	2,400	2,150	2,200	2,505	3,220
	14,180	15,470	13,810	14,406	17,220
Plant					
Unexpended—designated	3,769	2,125	1,460	620	550
Unexpended—restricted	11,875	12,680	7,452	2,165	1,210
Investment in plant	27,650	28,220	33,159	36,540	38,210
	43,294	42,985	42,070	39,333	39,970
Total	$59,154	$60,050	$57,265	$55,117	$58,962

External Auditor's Report

The final step in this annual process of financial responsibility and financial approval is the presentation of a statement prepared by external auditors, either state auditors or a public accounting firm. This annual audit is prepared in accordance with generally accepted accounting principles that (1) have been approved by the American Institute of Certified Public Accountants in its industry audit guide *Audits of Colleges and Universities*, (2) have been promulgated by the industry (in this case, higher education) in NACUBO's *College and University Business Administration* (1974), (3) have been adopted by the National Center for Education Statistics for financial reporting to the federal government, and (4) are compatible with the program classification structure developed by the National Center for Higher Education Management Systems.

Formats of the annual audited report are included in the next section, "Illustrative Exhibits." These formats, which primarily reflect fiduciary responsibility, are not identical to those presented in Report Nos. 15-18, but they are compatible with them and can be cross-referenced.

This final step, the audited report, is very important because it enables the board to know, from a source external to the institution, that the annual financial reports, as provided by management, have been reviewed by an external, independent body. The management letter, which accompanies the audited report, assures the trustees that not only are the figures accurate, but that the accounting systems are reliable.

Self-Evaluation

The above description completes the basic cycle that is necessary in all institutions. There are many other reports that may be needed and that should be used, depending on the type of institution, interest of the board, and priorities or problems that must be addressed on a continuing basis or at a particular time. Such additional reports may include those on cash flow, sponsored projects, insurance coverage, outstanding debt obligations, and unit costs of instruction. Although many more could be added, it is hoped that the ones presented here will provide a basis for the governing board to decide what reports will be most useful to it in planning the institution's future.

This monograph emphasizes "best practice" in defining the financial responsibilities of governing boards and the ways in which financial information may be presented. It is recognized that the "best practice" approach presented here may appear to be overwhelming. What is important, however, is to be assured that the board is carrying out its financial responsibilities in maintaining the institution's mission while incurring a prudent level of risk.

If it is assumed that the "best practices" described in this monograph may be of benefit to most colleges and universities, there should be some method by which the proposed concepts are examined, tested, and evaluated to determine their merit at a particular institution. This can be done.

A recommended method is for the chairperson of the board, the president, and the chief business officer to initially review the monograph and to determine its merit for the institution. In fact, the monograph could serve as a check list to determine how effectively the institution is communicating with the board. Based on the initial observations, one or more of the following decisions might be made:

- No action is required because present policies and practices are satisfactory.
- Certain policies and/or practices should be altered immediately.
- Other issues will require further study.

For the issues requiring further study, the chairperson of the board and the president may wish to appoint a self-evaluation panel. This panel could be charged with comparing the institution's financial policies and information systems with those outlined in the monograph. The panel should have broad representation to insure a variety of participation in the evaluation process. Major variances should be noted and analyzed to determine if any policies and practices should be changed. The chief business officer can be helpful in evaluating current reporting practices and in suggesting to the panel possible areas for improvement.

There will be many instances where existing policies and practices will be superior to those contained in the monograph because they are tailored to the specific traditions, characteristics, and needs of the institution. Even for these institutions, this monograph should serve as a stimulus for improved governance.

Illustrative Exhibits

The figures used in the accompanying exhibits are illustrative only and are not intended to indicate any relationship among accounts. The summary of significant accounting policies and notes to financial statements relate to the illustrative statements. Modifications should be made thereto as appropriate to actual circumstances.

Material from the Industry Audit Guide, *Audits of Colleges and Universities,* copyright © 1973 by the American Institute of Certified Public Accountants, Inc., and from *College and University Business Administration,* copyright © 1974 by NACUBO, is adapted with permission.

Exhibit A
Balance Sheet

June 30, 19
with comparative figures at June 30, 19
Sample Educational Institution

Assets	Current Year	Prior Year
Current Funds		
Unrestricted		
Cash	$ 210,000	$ 110,000
Investments	450,000	360,000
Accounts receivable, less allowance of $18,000 both years	228,000	175,000
Inventories, at lower of cost (first-in, first-out basis) or market	90,000	80,000
Prepaid expenses and deferred charges	28,000	20,000
Total unrestricted	1,006,000	745,000
Restricted		
Cash	145,000	101,000
Investments	175,000	165,000
Accounts receivable, less allowance of $8,000 both years	68,000	160,000
Unbilled charges	72,000	—
Total restricted	460,000	426,000
Total current funds	1,466,000	1,171,000
Loan Funds		
Cash	30,000	20,000
Investments	100,000	100,000
Loans to students, faculty, and staff, less allowance of $10,000 current year and $9,000 prior year	550,000	382,000
Due from unrestricted funds	3,000	—
Total loan funds	683,000	502,000
Endowment and Similar Funds		
Cash	100,000	101,000
Investments	13,900,000	11,800,000
Total endowment and similar funds	14,000,000	11,901,000

Liabilities and Fund Balances	Current Year	Prior Year
Current Funds		
Unrestricted		
Accounts payable	$ 125,000	$ 100,000
Accrued liabilities	20,000	15,000
Students' deposits	30,000	35,000
Due to other funds	158,000	120,000
Deferred credits	30,000	20,000
Fund balance	643,000	455,000
Total unrestricted	1,006,000	745,000
Restricted		
Accounts payable	14,000	5,000
Fund balance	446,000	421,000
Total restricted	460,000	426,000
Total current funds	1,466,000	1,171,000
Loan Funds		
Fund balances		
U.S. government grants refundable	50,000	33,000
University funds		
Restricted	483,000	369,000
Unrestricted	150,000	100,000
Total loan funds	683,000	502,000
Endowment and Similar Funds		
Fund balances		
Endowment	7,800,000	6,740,000
Term endowment	3,840,000	3,420,000
Quasi-endowment—unrestricted	1,000,000	800,000
Quasi-endowment—restricted	1,360,000	941,000
Total endowment and similar funds	14,000,000	11,901,000

Assets			Liabilities and Fund Balances		
Annuity and Life Income Funds			**Annuity and Life Income Funds**		
	Current Year	**Prior Year**		**Current Year**	**Prior Year**
Annuity funds			**Annuity funds**		
Cash	$ 55,000	$ 45,000	Annuities payable	$ 2,150,000	$ 2,300,000
Investments	3,260,000	3,010,000	Fund balances	1,165,000	755,000
Total annuity funds	3,315,000	3,055,000	Total annuity funds	3,315,000	3,055,000
Life income funds			**Life income funds**		
Cash	15,000	15,000	Income payable	5,000	5,000
Investments	2,045,000	1,740,000	Fund balances	2,055,000	1,750,000
Total life income funds	2,060,000	1,755,000	Total life income funds	2,060,000	1,755,000
Total annuity and life income funds	5,375,000	4,810,000	Total annuity and life income funds	5,375,000	4,810,000
Plant Funds			**Plant Funds**		
Unexpended			**Unexpended**		
Cash	275,000	410,000	Accounts payable	10,000	—
Investments	1,285,000	1,590,000	Notes payable	100,000	—
Due from unrestricted current funds	150,000	120,000	Bonds payable	400,000	—
			Fund balances		
			Restricted	1,000,000	1,860,000
			Unrestricted	200,000	260,000
Total unexpended	1,710,000	2,120,000	Total unexpended	1,710,000	2,120,000
Renewals and replacements			**Renewals and replacements**		
Cash	5,000	4,000	Fund balances		
Investments	150,000	286,000	Restricted	25,000	180,000
Deposits with trustees	100,000	90,000	Unrestricted	235,000	200,000
Due from unrestricted current funds	5,000	—			
Total renewals and replacements	260,000	380,000	Total renewals and replacements	260,000	380,000
Retirement of indebtedness			**Retirement of indebtedness**		
Cash	50,000	40,000	Fund balances		
Deposits with trustees	250,000	253,000	Restricted	185,000	125,000
			Unrestricted	115,000	168,000
Total retirement of indebtedness	300,000	293,000	Total retirement of indebtedness	300,000	293,000
Investment in plant			**Investment in plant**		
Land	500,000	500,000	Notes payable	790,000	810,000
Land improvements	1,000,000	1,110,000	Bonds payable	2,200,000	2,400,000
Buildings	25,000,000	24,060,000	Mortgages payable	400,000	200,000
Equipment	15,000,000	14,200,000	Net investment in plant	38,210,000	36,540,000
Library books	100,000	80,000			
Total investment in plant	41,600,000	39,950,000	Total investment in plant	41,600,000	39,950,000
Total plant funds	43,870,000	42,743,000	Total plant funds	43,870,000	42,743,000
Agency Funds			**Agency Funds**		
Cash	50,000	70,000	Deposits held in custody for others	110,000	90,000
Investments	60,000	20,000			
Total agency funds	110,000	90,000	Total agency funds	110,000	90,000

See accompanying Summary of Significant Accounting Policies and Notes to Financial Statements

Exhibit D
Statement of Changes in Fund Balances

Year Ended June 30, 19__
Sample Educational Institution

	Current Funds		Loan Funds	Endowment and Similar Funds	Annuity and Life Income Funds	Plant Funds			
	Unrestricted	Restricted				Unexpended	Renewals and Replacements	Retirement of Indebtedness	Investment in Plant
Revenues and Other Additions									
Unrestricted current fund revenues	$7,540,000								
Expired term endowment—restricted						$ 50,000			
State appropriations—restricted						50,000			
Federal grants and contracts—restricted		$ 500,000							
Private gifts, grants, and contracts—restricted		370,000	$100,000	$1,500,000	$800,000	115,000		$65,000	$ 15,000
Investment income—restricted		224,000	12,000	10,000		5,000	$ 5,000	5,000	
Realized gains on investments—unrestricted				109,000					
Realized gains on investments—restricted			4,000	50,000		10,000	5,000	5,000	
Interest on loans receivable			7,000						
U.S. government advances			18,000						
Expended for plant facilities (including $100,000 charged to current funds expenditures)									1,550,000
Retirement of indebtedness									220,000
Accrued interest on sale of bonds								3,000	
Matured annuity and life income restricted to endowment				10,000					
Total revenues and other additions	7,540,000	1,094,000	141,000	1,670,000	800,000	230,000	10,000	78,000	1,785,000
Expenditures and Other Deductions									
Educational and general expenditures	4,400,000	1,014,000							
Auxiliary enterprises expenditures	1,830,000								
Indirect costs recovered		35,000							
Refunded to grantors		20,000	10,000						
Loan cancellations and write-offs			1,000						
Administrative and collection costs			1,000					1,000	
Adjustment of actuarial liability for annuities payable					75,000				
Expended for plant facilities (including noncapitalized expenditures of $50,000)						1,200,000	300,000		
Retirement of indebtedness								220,000	
Interest on indebtedness								190,000	
Disposal of plant facilities									15,000
Expired term endowments ($40,000 unrestricted, $50,000 restricted to plant)				90,000					
Matured annuity and life income funds restricted to endowment				10,000					
Total expenditures and other deductions	6,230,000	1,069,000	12,000	90,000	85,000	1,200,000	300,000	411,000	15,000

	Current Funds		Loan Funds	Endowment and Similar Funds	Annuity and Life Income Funds	Plant Funds			
	Unrestricted	Restricted				Unexpended	Renewals and Replacements	Retirement of Indebtedness	Investment in Plant
Transfers Among Funds—Additions/(Deductions)									
Mandatory:									
Principal and interest	(340,000)							340,000	
Renewals and replacements	(170,000)						170,000		
Loan fund matching grant	(2,000)		2,000						
Unrestricted gifts allocated	(650,000)		50,000	550,000		50,000			
Portion of unrestricted quasi-endowment funds investment gains appropriated	40,000			(40,000)					
Total transfers	(1,122,000)		52,000	510,000		50,000	170,000	340,000	
Net increase/(decrease) for the year	188,000	25,000	181,000	2,099,000	715,000	(920,000)	(120,000)	7,000	1,670,000
Fund balance at beginning of year	455,000	421,000	502,000	11,901,000	2,505,000	2,120,000	380,000	293,000	36,540,000
Fund balance at end of year	643,000	446,000	683,000	14,000,000	3,220,000	1,200,000	260,000	300,000	38,210,000

See accompanying Summary of Significant Accounting Policies and Notes to Financial Statements

Exhibit C
Statement of Current Funds Revenues, Expenditures, and Other Changes

Year Ended June 30, 19
Sample Educational Institution

	Current Year Unrestricted	Restricted	Total	Prior Year Total
Revenues				
Tuition and fees	$2,600,000		$2,600,000	$2,300,000
Federal appropriations	500,000		500,000	500,000
State appropriations	700,000		700,000	700,000
Local appropriations	100,000		100,000	100,000
Federal grants and contracts	20,000	$ 375,000	395,000	350,000
State grants and contracts	10,000	25,000	35,000	200,000
Local grants and contracts	5,000	25,000	30,000	45,000
Private gifts, grants, and contracts	850,000	380,000	1,230,000	1,190,000
Endowment income	325,000	209,000	534,000	500,000
Sales and services of educational activities	190,000		190,000	195,000
Sales and services of auxiliary enterprises	2,200,000		2,200,000	2,100,000
Expired term endowment	40,000		40,000	
Other sources (if any)				
Total current revenues	7,540,000	1,014,000	8,554,000	8,180,000
Expenditures and mandatory transfers				
Educational and general				
Instruction	2,960,000	489,000	3,449,000	3,300,000
Research	100,000	400,000	500,000	650,000
Public service	130,000	25,000	155,000	175,000
Academic support	250,000		250,000	225,000
Student services	200,000		200,000	195,000
Institutional support	450,000		450,000	445,000
Operation and maintenance of plant	220,000		220,000	200,000
Scholarships and fellowships	90,000	100,000	190,000	180,000
Educational and general expenditures	4,400,000	1,014,000	5,414,000	5,370,000
Mandatory transfers for:				
Principal and interest	90,000		90,000	50,000
Renewals and replacements	100,000		100,000	80,000
Loan fund matching grant	2,000		2,000	
Total educational and general	4,592,000	1,014,000	5,606,000	5,500,000
Auxiliary enterprises				
Expenditures	1,830,000		1,830,000	1,730,000
Mandatory transfers for:				
Principal and interest	250,000		250,000	250,000
Renewals and replacements	70,000		70,000	70,000
Total auxiliary enterprises	2,150,000		2,150,000	2,050,000
Total expenditures and mandatory transfers	6,742,000	1,014,000	7,756,000	7,550,000
Other transfers and additions/(deductions)				
Excess of restricted receipts over transfers to revenues		45,000	45,000	40,000
Refunded to grantors		(20,000)	(20,000)	
Unrestricted gifts allocated to other funds	(650,000)		(650,000)	(510,000)
Portion of quasi-endowment gains appropriated	40,000		40,000	
Net increase in fund balances	188,000	25,000	213,000	160,000

See accompanying Summary of Significant Accounting Policies and Notes to Financial Statements

Summary of Significant Accounting Policies

June 30, 19____
Sample Educational Institution

The significant accounting policies followed by Sample Educational Institution are described below to enhance the usefulness of the financial statements to the reader.

Accrual Basis

The financial statements of Sample Educational Institution have been prepared on the accrual basis except for depreciation accounting as explained in notes 1 and 2 to the financial statements. The statement of current funds revenues, expenditures, and other changes is a statement of financial activities of current funds related to the current reporting period. It does not purport to present the results of operations or the net income or loss for the period as would a statement of income or a statement of revenues and expenses.

To the extent that current funds are used to finance plant assets, the amounts so provided are accounted for as (1) expenditures, in the case of normal replacement of movable equipment and library books; (2) mandatory transfers, in the case of required provisions for debt amortization and interest and equipment renewal and replacement; and (3) transfers of a nonmandatory nature for all other cases.

Fund Accounting

In order to ensure observance of limitations and restrictions placed on the use of the resources available to the Institution, the accounts of the Institution are maintained in accordance with the principles of "fund accounting." This is the procedure by which resources for various purposes are classified for accounting and reporting purposes into funds that are in accordance with activities or objectives specified. Separate accounts are maintained for each fund; however, in the accompanying financial statements, funds that have similar characteristics have been combined into fund groups. Accordingly, all financial transactions have been recorded and reported by fund group.

Within each fund group, fund balances restricted by outside sources are so indicated and are distinguished from unrestricted funds allocated to specific purposes by action of the governing board. Externally restricted funds may only be utilized in accordance with the purposes established by the source of such funds and are in contrast with unrestricted funds over which the governing board retains full control to use in achieving any of its institutional purposes.

Endowment funds are subject to the restrictions of gift instruments requiring in perpetuity that the principal be invested and the income only be utilized. Term endowment funds are similar to endowment funds except that upon the passage of a stated period of time or the occurrence of a particular event, all or part of the principal may be expended. While quasi-endowment funds have been established by the governing board for the same purposes as endowment funds, any portion of quasi-endowment funds may be expended.

All gains and losses arising from the sale, collection, or other disposition of investments and other noncash assets are accounted for in the fund which owned such assets. Ordinary income derived from investments, receivables, and the like is accounted for in the fund owning such assets, except for income derived from investments of endowment and similar funds, which income is accounted for in the fund to which it is restricted or, if unrestricted, as revenues in unrestricted current funds.

All other unrestricted revenue is accounted for in the unrestricted current fund. Restricted gifts, grants, appropriations, endowment income, and other restricted resources are accounted for in the appropriate restricted funds. Restricted current funds are reported as revenues and expenditures when expended for current operating purposes.

Other Significant Accounting Policies

Other significant accounting policies are set forth in the financial statements and the notes thereto.

Notes to Financial Statements

June 30, 19

Sample Educational Institution

1. Investments exclusive of physical plant are recorded at cost; investments received by gift are carried at market value at the date of acquisition. Quoted market values of investments (all marketable securities) of the funds indicated were as follows:

	Current year	Prior year
Unrestricted current funds	$ 510,000	$ 390,000
Restricted current funds	180,000	165,000
Loan funds	105,000	105,000
Unexpended plant funds	1,287,000	1,600,000
Renewal and replacement funds	145,000	285,000
Agency funds	60,000	20,000

Investments of endowment and similar funds and annuity and life income funds are composed of the following:

	Carrying value	
	Current year	Prior year
Endowment and similar funds:		
Corporate stocks and bonds (approximate market, current year $15,000,000, prior year $10,900,000)	$13,000,000	$10,901,000
Rental properties—less accumulated depreciation, current year $500,000, prior year $400,000	900,000	899,000
	13,900,000	11,800,000
Annuity funds:		
U.S. bonds (approximate market, current year $200,000 prior year $100,000)	200,000	110,000
Corporate stocks and bonds (approximate market, current year $3,070,000, prior year $2,905,000)	3,060,000	2,900,000
	3,260,000	3,010,000
Life income funds:		
Municipal bonds (approximate market, current year $1,400,000, prior year $1,340,000)	1,500,000	1,300,000
Corporate stocks and bonds (approximate market, current year $650,000, prior year $400,000)	545,000	440,000
	2,045,000	1,740,000

Assets of endowment funds, except nonmarketable investments of term endowment having a book value of $200,000 and quasi-endowment having a book value of $800,000, are pooled on a market value basis, with each individual fund subscribing to or disposing of units on the basis of the value per unit at market value at the beginning of the calendar quarter within which the transaction takes place. Of the total units each having a market value of $15.00, 600,000 units were owned by endowment, 280,000 units by term endowment, and 120,000 units by quasi-endowment at June 30, 19_____.

The following tabulation summarizes changes in relationships between cost and market values of the pooled assets:

	Pooled Assets		Net Gains (Losses)	Market Value per Unit
	Market	Cost		
End of year	$15,000,000	$13,000,000	$2,000,000	$15.00
Beginning of year	10,900,000	10,901,000	(1,000)	12.70
Unrealized net gains for year			2,001,000	
Realized net gains for year			159,000	
			$2,160,000	2.30

The average annual earnings per unit, exclusive of net gains, were $.56 for the year.

2. Physical plant and equipment are stated at cost at date of acquisition or fair value at date of donation in the case of gifts, except land acquired prior to 1940, which is valued at appraisal value in 1940 at $300,000. Depreciation on physical plant and equipment is not recorded.
3. Long-term debt includes: bonds payable due in annual installments varying from $45,000 to $55,000 with interest at 5¾%, the final installment being due in 19_____, collateralized by trust indenture covering land, buildings, and equipment known as Smith dormitory carried in the accounts at $2,500,000, and pledged net revenue from the operations of said dormitory; and mortgages payable due in varying amounts to 19_____ with interest at 6%, collateralized by property carried in the accounts at $800,000 and pledged revenue of the Student Union amounting to approximately $65,000 per year.
4. The Institution has certain contributory pension plans for academic and nonacademic personnel. Total pension expense for the year was $350,000, which includes amortization of prior service cost over a period of 20 years. The Institution's policy is to fund pension costs accrued, including periodic funding of prior years' accruals not previously funded. The actuarially computed value of vested benefits as of June 30, 19_____ exceeded net assets of the pension fund by approximately $300,000.
5. Contracts have been let for the construction of additional classroom buildings in the amount of $3,000,000. Construction and equipment are estimated to aggregate $5,000,000, which will be financed by available resources and an issue of bonds payable over a period of 40 years amounting to $4,000,000.
6. All interfund borrowings have been made from unrestricted funds. The amounts due to plant funds from current unrestricted funds are payable within one year without interest. The amount due to loan funds from current unrestricted funds is payable currently.
7. Pledges totaling $260,000, restricted to plant fund uses, are due to be collected over the next three fiscal years in the amounts of $120,000, $80,000, and $60,000, respectively. It is not practicable to estimate the net realizable value of such pledges.

Glossary

Accreditation: The granting of approval to a college or university by an official review board after the institution has met specific requirements. Institutional accreditation is carried out by regional accrediting associations; program accreditation (for example, music) is carried out by specialized associations (for example, National Association of Schools of Music).

Agency Funds: Resources held by an institution as custodian or fiscal agent for individual students, faculty, staff members, and organizations.

Aging of Receivables: Analysis of individual accounts receivable according to the time elapsed after the date of billing or the due date, usually the former.

Annuity Agreement: An agreement whereby money or other property is made available to an institution on the condition that the institution bind itself to pay periodically to the donor or other designated individuals stipulated amounts, which payments are to terminate at a time specified in the agreement.

Annuity Funds: Funds acquired by an institution subject to annuity agreements (*q.v.*).

Appropriation: An expenditure authorization with specific limitations as to amount, purpose, and time; a formal advance approval of an expenditure from designated resources available or estimated to be available.

Auxiliary Enterprise: An entity that furnishes a service directly or indirectly to students, faculty, or staff, and charges a fee directly related to, but not necessarily equal to, the cost of the service. The public may be served incidentally by some auxiliary enterprises. The services are essential elements in support of the institution's program, and conceptually should be regarded as self-supporting.

Bequest: Property received through a will; restrictions may or may not attach to use of the property.

Book Value (of Assets): Purchase price of an asset less any accumulated depreciation; in the case of an asset received as a gift, the appraised market value of the asset as of the date donated less any accumulated depreciation.

Budget: A statement of proposed expenditures for a fixed period or for a specific project or program, and the proposed means of financing the expenditures.

Carnegie Classification: A classification of institutions of higher education, first published in 1973 by the Carnegie Commission on Higher Education and revised in 1976 by the successor Carnegie Council on Policy Studies in Higher Education. It groups institutions into the following categories: doctoral-granting (four subgroups), comprehensive universities and colleges (two subgroups), liberal arts colleges (two subgroups), two-year colleges and institutes, professional and other specialized institutions (nine subgroups), and institutions for nontraditional study.

Current Funds: Resources to be expended in the near term and used for operating purposes.

Debt Financing: Acquisition of an asset by borrowing money, thereby creating a liability; typical forms of debt financing are loans and mortgages.

Debt Service: All payments in connection with funds borrowed by an institution: principal payments, interest charges, payments to sinking funds to insure future principal and interest payments, payments to reserves to insure proper upkeep and maintenance of the facilities, trustees' service charges, legal expenses, and other items related to indebtedness.

Deferred (or Unearned) Revenue: That portion of receipts for which services have not been completely performed, e.g., food service payments. Until such services are performed in their entirety, that portion of the receipts is considered a liability.

Designated Funds: Unrestricted resources expendable only for purposes designated by the governing board. (Also see *Undesignated Funds*.)

Endowment Funds: Funds which a donor or other outside agency has stipulated, as a condition of the gift, that the principal is to be maintained inviolate and in perpetuity and that only the income from the investments of the fund may be expended.

Endowment Income: Yield, usually in the form of interest and dividends, which occurs as a result of investing the principal of an endowment fund. Capital gains and losses are not a part of endowment income. (Also see *Total Return*.)

Fellowships: Financial assistance to graduate or postgraduate students, based primarily on academic achievement and vocational and professional objectives. Recipients are not required to render service to the institution as a consideration for their aid, nor are they required to repay. (Also see *Scholarships*.)

Full-time Equivalent (FTE): A means for expressing part-time students or faculty in terms of full-time. The formula is generally based on credit hours; for example, an institution may define full-time as being 12 credit hours, so a student (or faculty member) taking (or teaching) three credit hours would then be a .25 FTE.

Fund Accounting: A sum of money and other assets constituting a separate accounting entity, created and maintained for a particular purpose and having transactions subject to legal or administrative limitations. Its double-entry accounts are self-balancing, and from there a balance sheet and operating statement may be prepared.

Fund Balance: The difference between assets and liabilities in a fund group (*q.v.*).

Fund Group: A group of resources having similar purposes; typical fund groups in colleges and universities are current, loan, endowment and similar, annuity and life income, plant, and agency.

Graduate Record Examination (GRE): An examination taken by undergraduates in their major field as part of the admission requirements for most graduate institutions.

Indirect Costs: Costs that have been incurred for purposes common to a number or all of the specific projects, programs, or activities of an institution, but which cannot be identified and charged directly to such projects, programs, or activities relatively easily with a reasonable degree of accuracy and without an inordinate amount of accounting. Examples include such items as heating, lighting, air conditioning, and janitorial services of buildings, and administrative services such as accounting, purchasing, personnel, and library services.

Internal Auditing: A review of operations within established policy guidelines, which provides managers with reports, conclusions, and recommendations of the results of the review; it is an element of managerial control for measuring and evaluating the effectiveness of such control within the organization.

Life Income Agreement: An agreement whereby money or other property is made available to an institution on the condition that the institution bind itself to pay periodically to the donor or other designated individual(s) the income earned by the assets donated to the institution for the lifetime of the donor or of the designated individual(s).

Life Income Funds: Funds acquired by an institution subject to life income agreements (*q.v.*).

Loan Funds: Funds to be lent to students, faculty, or staff. When both principal and interest on the

loans are lendable, they are included in the Loan Funds group. If only the income from a fund is lendable, the principal is included in the Endowment and Similar Funds group, while the cumulative income constitutes the loan fund.

Mandatory Transfers: Transfers arising out of (1) binding legal agreements related to the financing of educational plant, such as amounts for debt retirement, interest, and required provisions for renewals and replacements of plant, not financed from other sources, and (2) grant agreements with agencies of the federal government, donors, and other organizations to match gifts and grants to Loan Funds and other funds. (Also see *Nonmandatory Transfers.*)

Nonmandatory Transfers: Transfers to other fund groups made at the discretion of the governing board to serve a variety of objectives, such as additions to loan funds, additions to quasi-endowment funds, general or specific plant additions, voluntary renewals and replacements of plant, and prepayments on debt principal. (Also see *Mandatory Transfers.*)

Payout Rate: (See *Spending Policy.*)

Plant Funds: Funds to be used for the construction, rehabilitation, and acquisition of physical properties for institutional purposes; funds already expended for such properties; funds set aside for the renewal and replacement thereof; and funds accumulated for the retirement of indebtedness thereon.

Pooled Investments: Fund assets pooled or consolidated for investment purposes.

Quasi-endowment Funds: Funds which the governing board, rather than a donor or other outside agency, has determined are to be retained and invested. The governing board has the right to decide at any time to expend such funds. Sometimes referred to as funds functioning as endowment.

Reserve: An account that records a portion of the fund balance that is allocated or set aside for some eventuality or future use and is thus not otherwise available.

Restricted Funds: Funds limited to a specific use by outside agencies or persons, as distinguished from funds over which the institution has complete control and freedom as to use. (Also see *Unrestricted Funds.*)

Retention: The number of students returning to the institution, typically expressed as a percentage, e.g., seniors/original freshman class.

Sabbatical: A leave of absence, often with pay, granted to a professor, generally for a year at a time, for every six or seven years of continuous service. The primary purpose of such leave is for research or other forms of academic pursuit.

Scholarships: Financial assistance to undergraduate students, generally based on scholastic achievement and/or financial need. Recipients of scholarships are not required to render service or to reimburse the institution in return. (Also see *Fellowships.*)

Sinking Fund: Cash or other assets, and the interest or other income earned thereon, set apart for the retirement of a debt or for the protection of an investment in depreciable property.

Spending Policy: In investing for total return (*q.v.*), the portion of earnings (expressed as a percentage of market value, sometimes called the "payout rate") for current operating purposes, where "earnings" includes the sum of net realized and unrealized appreciation or shrinkage in portfolio value plus yield (dividend and interest income). A prudent spending policy would protect the endowment from loss of purchasing power before appropriating gains.

Sponsored Projects: Projects performed in accordance with the conditions of agreements with governmental agencies or other outside organizations or persons to conduct activities of a specified scope.

Tenure: Permanence of position, often granted after a specified number of years.

Term Endowment: Funds which donors or other outside agencies, by the terms of the instrument of gift, have provided are to be released from inviolability to permit all or parts of them to be expended upon the happening of a particular event or the passage of a stated period of time. (Also see *Endowment Funds.*)

Total Return: The sum of net realized and unrealized appreciation or shrinkage in portfolio value plus yield (dividend and interest income).

Transfers: The moving of assets, liabilities, and balances from one fund group to another. (Also see *Mandatory Transfers* and *Nonmandatory Transfers.*)

True Endowment: (See *Endowment Funds.*)

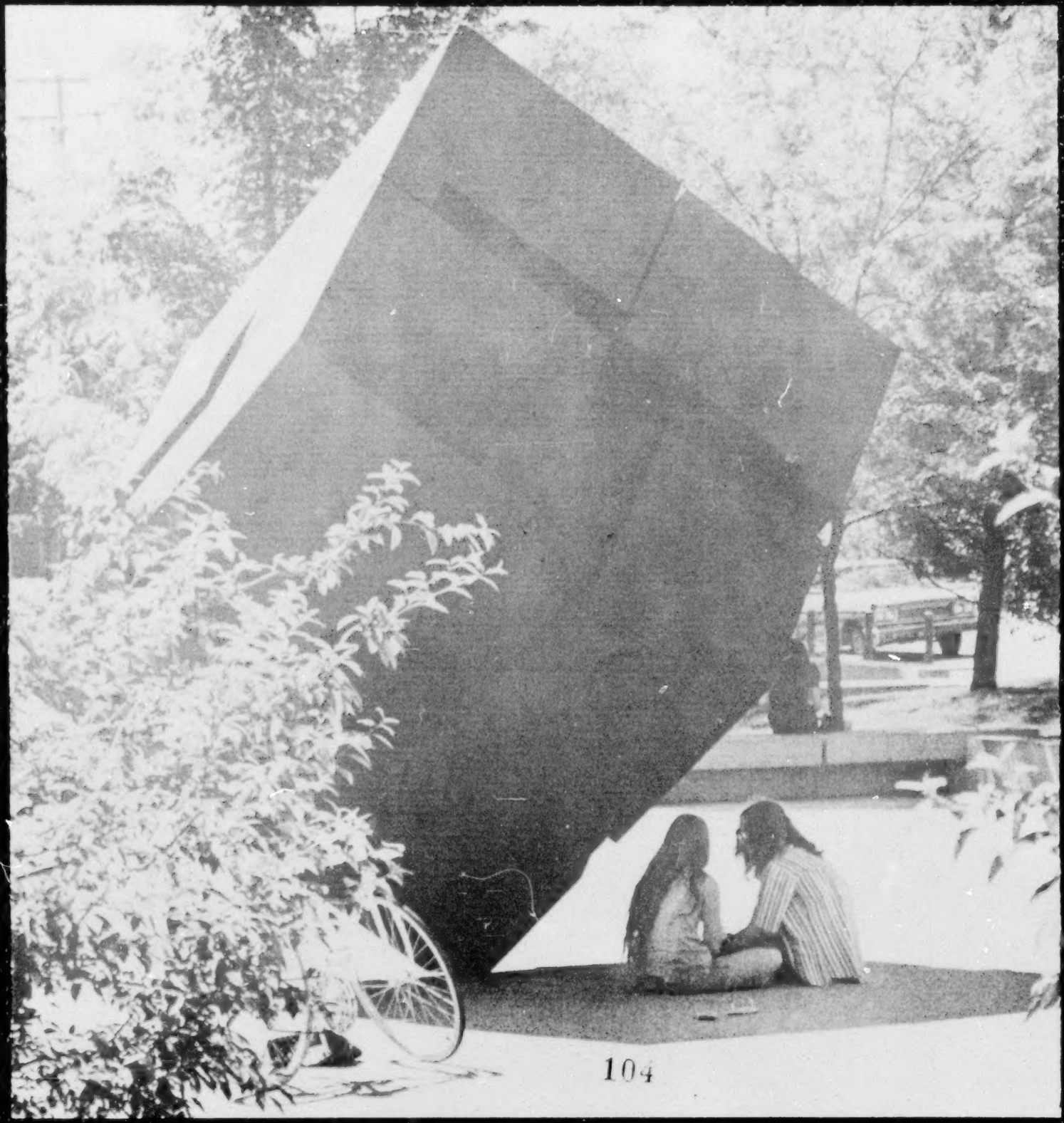
Trust: An agreement by which legal title to one's property is held by another party (trustee) for the future benefit of a designated beneficiary or beneficiaries. According to the terms of the agreement, trusts may be revocable or irrevocable.

Undesignated Funds: Unrestricted resources available for any purpose. (Also see *Designated Funds.*)

Unearned (or Deferred) Revenue: (See *Deferred (or Unearned) Revenue.*)

Unrestricted Funds: Resources provided to the institution with no restrictions on their use. (Also see *Restricted Funds.*)

Working Capital: Current fund cash, or current fund assets converted to cash, that will be used to liquidate current fund liabilities in a normal operating cycle, which is typically one year.



Bibliography

This selected bibliography is provided to assist readers who wish to explore in greater depth some of the issues addressed in the text. For information about these and other AGB and NACUBO publications, please write to the respective associations at the address on the copyright page.

Articles from *AGB Reports*

Bowman, William W. "Defer Maintenance, Invite Disaster." Vol. 19, no. 6 (Nov/Dec 1977), pp. 12-17.

Council for Financial Aid to Education. "Voluntary Support—Who Gets, Who Gives." Vol. 18, no. 5 (Sep/Oct 1976), pp. 24-25.

Dober, Richard P. "Save That College Building!" Vol. 18, no. 1 (Jan/Feb 1976), pp. 14-17.

Dozier, John M. "The Retrenchment Knife." Vol. 18, no. 1 (Jan/Feb 1976), pp. 10-13.

Ellis, R. L. "Managing the Endowment." Vol. 17, no. 5 (Mar/Apr 1975), pp. 11-15.

Embersits, John F. "A Save-Energy, Save-Money Program That Pays Off." Vol. 18, no. 3 (May/Jun 1976), pp. 15-19.

Hahn, Ralph C. "How We Cut Energy Consumption 25%." Vol. 20, no. 1 (Jan/Feb 1978), pp. 37-38.

Kemeny, John G. "Why I Might Refuse a Million-Dollar Gift." Vol. 20, no. 3 (May/June 1978), pp. 43-44. (Will it build the whole building? How will operating expenses be met?)

Murray, Roger F. "Endowment Funds and Moral Issues." Vol. 20, no. 4 (Jul/Aug 1978), pp. 5-8.

_____. "Making the Most of Your Endowment." Vol. 18, no. 4 (Jul/Aug 1976), pp. 7-12.

Seal, John C. "A Sensible Student Loan Formula." Vol. 18, no. 2 (Mar/Apr 1976), pp. 18-23.

Stuhr, Gonser G. T. "The Second Most Pressing Need." Vol. 20, no. 1 (Jan/Feb 1978), pp. 23-24. (A ten-step procedure for raising endowment gifts.)

(No author.) "Guidelines for Policies Affecting Potential Conflicts of Interest." Vol. 21, no. 1 (Jan/Feb 1979), pp. 31-34.

AGB Pamphlets (1977)

Chait, Richard P., and Ford, Andrew T. "The Tenure Issue."

Mortimer, Kenneth P. "Academic Collective Bargaining."

Nelson, Charles A. "Trustees and Resource Management."

Radock, Michael. "The Fund-Raising Role."

Woodruff, Bruce E. "Trustees Must Know the Law!"

AGB Booklets

E. D. Duryea with John C. Neddy *Collective Bargaining: Impact On Governance.* Washington, D.C.: Association of Governing Boards, 1977.

Nason, John W. *The Future of Trusteeship: The Role and Responsibilities of College and University Boards.* Washington, D.C.: Association of Governing Boards, 1975.

NACUBO Publications

Adams, John F. *Risk Management and Insurance: Guidelines for Higher Education* (1972).

College and University Business Administration (1974).

A College Planning Cycle (1975).

Energy Management for Colleges and Universities (1977).

Investment Policies and Procedures at Selected Colleges and Universities (1977).

Patent and Copyright Policies at Selected Colleges and Universities (1978).

"Reporting on Investments of Endowment Funds" (1975).

"Results of the 1977 NACUBO Comparative Performance Study and Investment Questionnaire" (1978). Annual.

Other Publications

Aiken, Ray J.; Adams, John F.; and Hall, John W. *Legal Liabilities in Higher Education: Their Scope and Management.* Washington, D.C.: Association of American Colleges, 1976.

Angell, George W. "Trustees and Collective Bargaining—Two Reports." ACBIS Monograph #5. Washington, D.C.: Academic Collective Bargaining Information Service, 1978.

Carnegie Commission on Higher Education. *Priorities for Action: Final Report of the Carnegie Commission on Higher Education.* New York: McGraw-Hill Book Co., 1973.

_____. *Governance of Higher Education.* New York: McGraw-Hill Book Co., 1973.

Hendrickson, Robert M., and Mangum, Ronald Scott. *Governing Board and Administrator Liability.* ERIC/Higher Education Research Report No. 9. Washington, D.C.: American Association for Higher Education, 1977.

Minter, John W., and Bowen, Howard R. *Fourth Annual Report on Financial and Educational Trends in the Private Sector of American Higher Education.* Washington, D.C.: Association of American Colleges, 1978. Annual.

Mood, Alexander M. *The Future of Higher Education. A Report Prepared for the Carnegie Commission on Higher Education.* New York: McGraw-Hill Book Co., 1973. (Contains extensive bibliography.)

Williamson, J. Peter. Background paper in *Funds for the Future: Report of the Twentieth Century Fund Task Force on College and University Endowment Policy.* New York: McGraw-Hill Book Co., 1975.

Association of Governing Boards of Universities and Colleges
One Dupont Circle
Suite 720
Washington, D.C. 20036
202/296-8400

National Association of College and University Business Officers
One Dupont Circle
Suite 510
Washington, D.C. 20036
202/296-2344